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## DOCTOR OF PHILOSOPHY

**Appropriate comparator in national treatment under international investment law  
relevance of GATT/WTO, EU and international human rights jurisprudences**

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# DOCTOR OF PHILOSOPHY

## Appropriate comparator in national treatment under international investment law:

*relevance of GATT/WTO, EU and international human rights jurisprudences*

Norfadhilah Mohamad Ali

2014

University of Dundee

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**Appropriate Comparator in National Treatment under International  
Investment Law: Relevance of GATT/WTO, EU and International Human  
Rights Jurisprudences**

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Norfadhilah Mohamad Ali

Dundee - November, 2013

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I, the candidate, hereby acknowledge:

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## **Thesis Abstract**

The minimalist state of the national treatment provision in the investment treaties has provided limited guidance for the tribunals for interpretation. As a result, there were inconsistencies in the interpretation of national treatment, in particular the question of likeness. This thesis aims to develop the doctrinal understanding of the determination of appropriate comparator guided by the underlying philosophies, historical evolution and relevant investment decisions. The methods applied in this thesis are doctrinal and comparative studies of international investment law and the compared jurisprudences. A major part of this thesis is dedicated to examine the comparison and relevance of the GATT/WTO, EU and international human rights law in the interpretation of discrimination based on nationality. The interpretative methods applied by the respective jurisprudences in determining likeness and related questions of legitimate regulatory measures are examined to see whether there are lessons that could be learnt in the interpretation of national treatment in investment law. The finding of this thesis confirms that there is potentially a range of insightful guidance from the jurisprudences under comparison which could provide a structured understanding of national treatment in international investment law. The observations put forth highlight the underlying philosophies and values of the national treatment principle in protecting the investors and addressing the host states' regulatory needs. It reflects the contemporaneous development in international investment law and provides a positive response to public administrative principles benefitted by way of international comparative administration law.

## **Abbreviations**

ACHPR	Protocol to the African Charter on the African Court on Human and Peoples' Rights
ACHR	American Convention of Human Rights
Canadian FIPAs	Canadian Foreign Investment Protection Agreements
DCS	Directly competitive or substitutable
DTCs	Double Tax Conventions
EC	European Community
ECHR	European Convention of Human Rights
EEC	European Economic Community
EU	European Union
EHRR	European Human Rights Reports
FCN	Treaty of Friendship, Commerce and Navigation
FIRA	Foreign Investment Review Act
FRC	Fundamental Rights Charter
GATT/WTO	General Agreement on Tariffs and Trade/ World Trade Organization
HFCS	High fructose corn syrup
ICCPR	International Covenant on Civil and Political Rights
ICCPR	The United Nations Convention on Civil and Political Rights
ICESCR	The United Nations Covenants on Economic, Social and Cultural Rights
ICJ	International Court of Justice
MAI	Multilateral Agreement on Investment

NAFTA	North American Free Trade Agreement
NTB	Non-tariff barriers
OECD	Organization for Economic Co-operation and Development
PCBc	Polychlorinated biphenyl
PPM	Product Process Doctrine
TRIMS	Trade-Related Investment Measures
TRIPs	Trade-Related Aspects of Intellectual Property Rights
UDHR	Universal Declaration of Human Rights
UNCTAD	United Nations Conference on Trade and Development
VCLT	Vienna Convention of the Law of Treaties



## **Table of International Treaties and Other Instruments**

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1929 Draft Convention on the Treatment of Foreigners, Proceedings of the International Conference on Treatment of Foreigners. First Session, Paris, November 5-December 5, 1929. Geneva, 1930. 573 p.33cm. (League of Nations, C-97.M.23. 1930. II.5).

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## **1988**

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## Chapter 1

### RESEARCH BACKGROUND

#### 1.0 Introduction

National treatment in international investment law is a doctrine aimed to prohibit host states from introducing discriminatory measures that favour domestic than foreign investors or investments, in like circumstances. It is a common provision found in almost all bilateral investment treaties and other international investment agreements.<sup>1</sup> The inclusion of this provision in international investment agreements and treaties provides an assurance to foreign investors that their investments will operate at least at a level playing field and at the course of ordinary business circumstances or risks.<sup>2</sup> It promotes the establishment of neutral investment environment and reduces discrimination, which would otherwise be a certain risk to foreign investors.<sup>3</sup>

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<sup>1</sup> Examples of investment treaties containing national treatment provision are UK-Argentina BIT , Egypt-Germany BIT (2005) , Korea- Malaysia BIT (1988) and Finland-Brazil BIT (1995) all text are available at <<http://www.unctadxi.org/templates/DocSearch.aspx?id=779>> , accessed on 28 July 2014. National treatment provisions are also inserted in the North American Free Trade Agreement (NAFTA) between the Government of Canada, the Government of Mexico and the Government of the United States, signed 17 December 1992, Can. T.S. 1994 [entered into force 1 January 1994], <<https://www.nafta-sec-alena.org/Default.aspx?tabid=97&ctl=FullView&mid=1588&language=en-US>>, accessed on 26 September 2013; and The Energy Charter Treaty, Annex 1, Official Journal of the European Communities, L69/26, March 1998, <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:1998:069:0026:0090:EN:PDF>>, accessed on 29 July 2013.

<sup>2</sup> Kenneth J Vandevelde, *Bilateral Investment Treaties: History, Policy, and Interpretation* (OUP USA 2010) 342.

<sup>3</sup> Thomas W Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (2004). Lord Mustill International Arbitration Conference. St. John's College.

The exposure of foreign investments to discrimination is a concern attributable to the host states' tendency in protecting its domestic investors against threats of competition in the open market.<sup>4</sup> Host states often find it hard to reconcile the limited regulatory function and the increasing internal pressure to safeguard national investors and strategic industries in facing competition with the foreign investors. A treatment which is favourable to national investors would probably be discriminatory to foreign investors. Such favourable treatments are commonly given through the change of fiscal regulations in the form of exemption of permits, rebates on taxes or less procedural requirements arising from the new regulations introduced by the host states, executed by governmental bodies or agencies in performing their regulatory functions.<sup>5</sup>

The states and their increasing regulatory function are termed as regulatory states. In the setting of a 'regulatory state', the state's role is shifted from controlling directly businesses or assets as a public entity ownership to a regulatory or supervisory role of the private owners of business.<sup>6</sup> It is by this function, and in the light of upholding the sovereignty to determine the state's own economic and social system that host states tend to impose rules and regulations to manage the important sectors in the state.

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<sup>4</sup> Governments seek through their regulations and administrative actions to assist their nationals and companies. See Jeswald Salacuse, *The Law of Investment Treaties* (Oxford University Press 2010) 245.

<sup>5</sup> The change of fiscal regulations and economic environment may adversely affect foreign investors. See Abba Kolo and Thomas W Walde, 'Coverage of Taxation Under Modern Investment Treaties' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (Oxford University Press 2008) 306.

<sup>6</sup> Giandomenico Majone, 'From the Positive to the Regulatory State: Causes and Consequences of Changes in the Mode of Governance' (1997) 17 *Journal of Public Policy* 139.

It is reported in the World Development Report 2005 that the regulations and taxes imposed by the host states tend to discriminate foreign investors, particularly by the developing countries.<sup>7</sup> The World Bank has also highlighted the potentials of how public ownership could weaken the investment climate, one of which is by setting up monopolies and denying opportunities to other firms. It claims that public enterprises often enjoy a range of exemptions either by law or by practice from taxes or regulations that can distort competition.<sup>8</sup>

The need to protect domestic investments became imminent due to huge inflow of foreign direct investments by privatisation encouraged by bilateral investment treaties (BITs) and regional and free trade treaties with investment chapters among states.<sup>9</sup> According to United Nations Conference on Trade and Development

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<sup>7</sup> World Development Report 2005, *A Better Investment Climate for Everyone* (The World Bank and Oxford University Press 2005) 96. See especially Figure 5.1: Low-income Countries Tend to Regulate More. Claims of discrimination also occur between OECD Member States and nationals of other OECD Member State, for instance those under NAFTA. See Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009) 53.

<sup>8</sup> World Development Report 2005, *A Better Investment Climate for Everyone* (n 7) 97.

<sup>9</sup> Privatisation has taken over public monopolies and caused the flow of foreign investment into the internal market in domains such as telecommunication, energy, water and transportation. Foreign direct investment inflow has reached a record in 2007, surpassing its previous peak in 2001 with inflows of \$1833 billion. Although the trend declined in 2008 due to the global and economic financial crisis, there was a modest recovery in early 2010. See United Nations Conference on Trade and Development (Geneva), *World Investment Report 2008: Transnational Corporations, and the Infrastructure Challenge* (United Nations 2008) 3.; United Nations Conference on Trade and Development, *World Investment Report 2010: Investing in a Low-Carbon Economy* (United Nations 2010) 2. For a recent update of the global foreign direct investment inflow, refer 'World Investment Report 2013: Global Value Chains: Investment and Trade for Development' (United Nations Conference on Trade and Development 2013) <[http://unctad.org/en/PublicationsLibrary/wir2013\\_en.pdf](http://unctad.org/en/PublicationsLibrary/wir2013_en.pdf)>, <[http://unctad.org/en/PublicationsLibrary/wir2013\\_en.pdf](http://unctad.org/en/PublicationsLibrary/wir2013_en.pdf)>, accessed on 26 September 2013. Privatisation has also contributed to the transformation of the international economy. See David J Donaldson, *Privatization: Principles and Practice* (World Bank Publications 1995) 9. As far as investment agreements involving more than two countries, the examples are North American Free Trade Agreement between the Government of Canada, the Government of Mexico and the Government of the United States (NAFTA), signed 17 December 1992, entered into force 1 January 1994], <<https://www.nafta-sec-alena.org/Default.aspx?tabid=97&ctl=FullView&mid=1588&language=en-US>>, accessed on 26 September 2013, The Energy Charter Treaty (ECT), [1998] OJ L69/26, <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:1998:069:0026:0090:EN:PDF>>, accessed on 29 July 2013.

(UNCTAD), there were 2608 BITs, 2730 double taxation treaties (DTTs) and 254 free trade agreement (FTA) by the end of 2008.<sup>10</sup> As these treaties guarantee extensive rights to the foreign investors against, inter alia expropriation, discrimination and unfair acts by the host states, they cast a huge responsibility on the host states to meet the obligations. This does not only mean that host states must ensure compliance of all domestic law before ratification of the treaties, but to maintain and work within the commitments which may involve future restrictions in introducing new measures into the domestic law.<sup>11</sup>

Due to the fragility of foreign investments against unpredictable regulatory changes which are potentially discriminatory, discrimination has become a more fearsome risk than other interferences, including formal expropriation.<sup>12</sup> The national treatment protection is an international discipline that counteracts innate tendencies of host states towards protectionism.<sup>13</sup>

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<sup>10</sup> UNCTAD also reported the increase of double taxation treaties and other international agreements with investment provisions. Refer UNCTAD, 'Recent Developments in International Investment Agreements (2008–June 2009)' (2009) xvii, <[http://www.unctad.org/en/docs/webdiaeia20098\\_en.pdf](http://www.unctad.org/en/docs/webdiaeia20098_en.pdf)>, accessed on 28 January 2014.

<sup>11</sup> More than four fifths (81.5%) of the 1,891 BITs that had entered into force until the end of 2005 became effective within the first three years after signature. This indicates the complicated process of national ratification required. Refer UNCTAD, 'The Entry into Force of Bilateral Investment Treaties (BITs)' (2006), <[http://www.unctad.org/en/docs/webiteia20069\\_en.pdf](http://www.unctad.org/en/docs/webiteia20069_en.pdf)>, accessed on 28 January 2014.

<sup>12</sup> Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3). Expropriation becomes an unpopular resort by states not only because of the uproar in such takings by capital exporters and the increase of investment cases at the tribunals but also because the important sectors have practically been taken over by states by 1970s. See also Vandeveld, *Bilateral Investment Treaties* (n 2), Michael S Minor, 'The Demise of Expropriation as an Instrument of LDC Policy, 1980-1992' (1994) 25 *Journal of International Business Studies* 177.

<sup>13</sup> Karl P Sauvart, 'FDI Protectionism Is on the Rise' [2009] *The World Bank*, <<http://elibrary.worldbank.org/content/workingpaper/10.1596/1813-9450-5052>> accessed on 14 October 2013.

## 2.0 Statement of Problem

Clauses on national treatment in international investment law instruments are almost identical, save for some wordings. Despite the similar nature of the national treatment provisions, there are inconsistencies in interpretation in the investment awards.<sup>14</sup> Among the most incoherent matters in national treatment are the identification of the relevant comparator -commonly phrased as ‘in like circumstances’ or ‘in like situations’ in national treatment provisions, the determination of legitimate regulatory measure and the comparative methodology in the interpretation of the national treatment provision.

### 2.1 Interpretation of Likeness in Investment Arbitration Cases

In determining the appropriate comparator, the tribunals took very divergent approaches from one case to another. The tribunal in the case of *Marvin Feldman v Mexico* limited likeness to only trading companies, excluding exporting companies even though they are similarly in the tobacco business.<sup>15</sup> The narrow approach taken was justified by the tribunal by holding that treating producers and resellers differently would promote *inter alia*; better control over tax revenue, discourage smuggling and prohibit grey market sales business.<sup>16</sup>

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<sup>14</sup> Rudolf Dolzer observed that it is misleading to assume that the homogeneity of the clauses make it easy for the standard to be applied. See Rudolf Dolzer, ‘National Treatment: New Developments’ (Symposium Co-organised by ICSID, OECD and UNCTAD 2005) <<http://www.oecd.org/daf/inv/internationalinvestmentagreements/36055356.pdf>>, accessed on 12 September 2013.

<sup>15</sup> *Marvin Feldman v Mexico* ICSID Case No. ARB(AF)/99/1, Award, 16 December 2002 (hereinafter ‘*Feldman v Mexico*’).

<sup>16</sup> *Ibid.*, para 172.

In contrast to *Feldman v Mexico*, the tribunal in *Occidental Exploration and Production Company v. Republic of Ecuador* adopted a broad interpretation to include all companies engaged in exports regardless of the sector they are in, as valid comparators to the claimant. Comparing the situation with ‘like product’ under the General Agreement on Tariffs and Trade (GATT/WTO),<sup>17</sup> the tribunal claimed that the case in question is broader, that no exporter is ought to be put in a disadvantageous position as compared to other exporters.<sup>18</sup> Thus, the tribunal concluded that the appropriate comparator could not be limited exclusively to the sector in which that particular activity is taken.

From the two cases, it can be observed that while the interpretation of likeness is very narrow in *Feldman v Mexico*, the tribunal captured the whole group of exporters ranging from flower exporters to oil exporters in the case of *OEPC v Ecuador*. In *Methanex Corporation v. United States of America*, in like circumstances was construed to be comparators who are in the ‘most’ like circumstances, not the ‘less’ like circumstances, particularly in the case where there is an identical comparator but for nationality which was not discriminated.<sup>19</sup> Having identical comparators producing methanol, the claimant was thus not considered as in like circumstances with other US domestic comparators producing oxygenates used in manufacturing reformulated gasoline that also compete for the same customers.

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<sup>17</sup> General Agreement on Tariffs and Trade (GATT), signed 1947, entered into force 1 January 1948, <[http://www.wto.org/english/docs\\_e/legal\\_e/gatt47\\_e.pdf](http://www.wto.org/english/docs_e/legal_e/gatt47_e.pdf)>, accessed on 5 October 2013.

<sup>18</sup> *Occidental Exploration and Production Company v The Republic of Ecuador* UNCITRAL, LCIA Case No UN3467, Final Award, 1 July 2004, para 176 (hereinafter ‘*OEPC v Ecuador*’).

<sup>19</sup> *Methanex Corporation v. United States of America* UNCITRAL/NAFTA, Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005, Part IV Chapter B p.8, para 17 (hereinafter ‘*Methanex v USA*’).

In the case of *Pope & Talbot Inc. v The Government of Canada*, in like circumstances was discussed in view of the location of comparators among softwood lumber exporters.<sup>20</sup> In that case, the producers in the non-covered provinces were considered as not in like circumstances with those in the covered provinces. In *United Parcel Service of America v Government of Canada*, the operation courier and postal services was considered to be not in like circumstances due to the difference in the delivery mechanism, where one was able to deliver to ‘large retail customer’ and ‘customers in shopping malls’ while the other one was a ‘home delivery service’.<sup>21</sup>

It is therefore observed that the interpretation of in like circumstances is construed differently and inconsistently by the tribunals which provides no predictability in the extent of the national treatment application.

## 2.2 The Need for a Set of Criteria for Likeness

The determination of likeness or appropriate comparator constitutes an integral test in invoking the national treatment protection.<sup>22</sup> Non-discrimination principle such as national treatment only prohibits between covered investment and certain selected

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<sup>20</sup> *Pope & Talbot Inc. v The Government of Canada* UNCITRAL/NAFTA, Award on the Merits of Phase 2, 10 April 2001, paras 75, 88 (hereinafter ‘*Pope & Talbot Inc. v Canada*’).

<sup>21</sup> *United Parcel Service of America Inc. v Canada* UNCITRAL/NAFTA, Award on the Merits, 24 May 2007 (hereinafter ‘*UPS v Canada*’).

<sup>22</sup> The two elements of national treatment analysis in Andrew Newcombe are (i) identifying the relevant comparator and (ii) comparing the treatment received by the foreign and local investor to determine whether there has been less favourable treatment. See Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 159. The importance of likeness and the difficulty of assessing it is a real issue in determining what constitute less favourable treatment to foreign investors. See AF. Maniruzzaman, ‘Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investments: An Overview’ (1998) 8 *Journal of Transnational Law and Policy*.



investments, termed ‘comparator’.<sup>23</sup> It has a direct causal relationship to the application of national treatment depending on the approach adopted. If a broad approach is applied, many investments would probably be regarded as like and thus makes the protection wider. On the contrary, if a narrow approach is applied, the scope will hence be smaller.

Having such an importance in national treatment, likeness has however not been developed in a manner which could cast light in the determination of guiding principles for comparison. It is observed that this absence is at least because of two reasons. Firstly, it is perceived as impossible to have one guide that applies to all investments, and secondly, that the matter should be left to be resolved by the arbitrators on a case by case basis.

The tribunals have suggested that the interpretation of likeness is context dependant, thus impossible to have a standard guide across all types of investments.<sup>24</sup> In *S.D. Myers Inc. v Canada*, the tribunal held that in like circumstances invites a very wide interpretation and depends highly to the context of a particular dispute.<sup>25</sup> Although factual circumstances are important in construing likeness, this thesis asserts that the criteria for likeness in investments are nevertheless possible. It is possible to characterise the vast diversity of investment, not necessarily solely by looking at the economic sector but by other relevant criteria congruent to investments.<sup>26</sup>

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<sup>23</sup> Vandevelde, *Bilateral Investment Treaties* (n 2) 338.

<sup>24</sup> *Pope & Talbot Inc. v Canada*, (n 20), para 75; *S.D. Myers Inc. v Government of Canada* UNCITRAL/ NAFTA, Partial Award, 13 November 2000 (hereinafter *SD Myers Inc. v Canada*), para 244.

<sup>25</sup> *S.D. Myers Inc. v Canada*, (n 24), para 244.

<sup>26</sup> Investments in the same economic sector is potentially a criteria of likeness. Likeness was construed in view of economic sector in some cases, see *S.D. Myers, Inc. v Canada*, (n 24) paras 243-251. Other relevant criteria to likeness in the investment context could be for instance, competition. Andrew Newcombe commented about the existence of a competitive relationship, which may

The existence of criteria for interpretation can be taken as example from other areas of international investment law like expropriation, or from other jurisprudences having similar protections.<sup>27</sup> International trade law acknowledges the complexity of determining the appropriate comparator. Gaeten Verhoosel described it as ‘one of the thorniest issues WTO panels has had to deal with in the past’.<sup>28</sup> Through the evolution of decided cases and lengthy scholarly discussions in GATT/WTO, the jurisprudence has developed certain characteristics or factors to determine appropriate comparator, namely the products’ end-users in a given market, consumers’ tastes and habits, the products’ property, nature and quality, the products’ tariff classification and the aim and effect test.<sup>29</sup> Similarity in approach is also observed in the EU law. The ECJ, in determining similar products for the purpose of Art 110 (1) TFEU (ex Article 90(1) EC) referred to whether the products were placed in the same classification, at the same stage of production or marketing, similar characteristics and meet the same needs from the viewpoint of consumers.<sup>30</sup> The competitive and substitutability factors are also examined in both jurisprudences.

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sometimes overlap or distinct from economic sector. See Andrew Newcombe (n 7)164. The competition criterion along with other criteria will be developed in this thesis in Ch.3 and 6.

<sup>27</sup> Criteria for expropriation are: (i) it must be for a public purpose (ii) it should be non-discriminatory (iii) it is taken in accordance with the applicable laws and due process (iv) full compensation is made. See Surya P Subedi, *International Investment Law: Reconciling Policy and Principle* (First Edition, Hart 2008) 74. See also Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (OUP Oxford 2008) 91. and *ADC Affiliate Limited and ADC & ADMC Management Limited v The Republic of Hungary*, ICSID Case No. ARB/03/16, Award, 2 October 2006, paras 429-433.

<sup>28</sup> Gaeten Verhoosel, *National Treatment and WTO Dispute Settlement: Adjudicating the Boundaries of Regulatory Autonomy* (Hart Publishing 2002) 23.

<sup>29</sup> In *Japan-Taxes on Alcoholic Beverages*, it was mentioned that no one approach will be appropriate for all cases. See Appellate Body Report, *Japan-Taxes on Alcoholic Beverages*, WT/DS8R, adopted 1 November 1996, page 21. Among the writers in the field are Robert Hudec, Gaeten Verhoosel, Rex Zedalis, Won Mog Choi, Federico Ortino, Nicholas Di Mascio, Joost Pauwelyn and Jurgen Kurtz. The scholarly articles will be referred to especially in the literature review in this chapter and the discussion on relevance of likeness in GATT/WTO in Ch.3.

<sup>30</sup> Case 27/67, *Firma Fink-Frucht GmbH v Hauptzollamt München-Landsbergerstrasse* [1968] ECR 223, para 232, Case 45/75, *Rewe-Zentrale des Lebensmittel-Großhandels GmbH v Hauptzollamt Landau/Pfalz* [1976] ECR 181, para 12.

The international investment jurisprudence on the other hand has no firm criteria that could classify investments for the purpose. Research must be conducted to provide a comprehensive observation as to what kind of circumstances which are considered alike in the investment environment.<sup>31</sup> The need of a set of criteria must not wait for the trend of arbitration awards which may take years and a long stretch of cases. Gabrielle Kaufman Kohler commented on the risk of waiting. The risk is that consistency will not emerge, as certain fundamental disagreements will remain.<sup>32</sup> With the current handful of inconsistent national treatment cases, it is hard to imagine elevating national treatment from ‘an empty shell’ standard to a systematic and consistent jurisprudence (*jurisprudence constante*), if the trend continues.<sup>33</sup>

### 2.3 Legitimate Regulatory Measure

Along with the interpretation of ‘in like circumstances’, the determination of legitimate policy objectives is also a potential area of incoherence. The question of legitimacy of government regulatory measure is closely inter-related to likeness. Tribunals will often not find a breach of national treatment if there is a justified policy reason for less favourable treatment. In other words, investments are considered ‘in like circumstances’ if there is no justified policy reason to treat them

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<sup>31</sup> It is not only about how to define likeness. The observation must be wide enough to encompass like circumstances. See *S.D. Myers, Inc. v Canada* (n 24) 250.

<sup>32</sup> Gabrielle Kaufmann-Kohler and International Arbitration Institute, ‘Is the Search of Consistency a Myth?’ in Emmanuel Gaillard and Yas Banifatemi (eds), *Precedent in International Arbitration* (Juris Publishing, Inc 2008).

<sup>33</sup> Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 148.

differently. As such, the determination of legitimate regulatory measure affects the interpretation of likeness.

The area of legitimate regulatory measure in the context of national treatment is still underdeveloped in international investment law. Unlike the expressed provision in the *chapeau* of Article XX GATT 1994 which exempts certain government discriminatory measures provided that they are not arbitrary or unjustifiable, the investment treaties generally do not provide such details.<sup>34</sup> The EU law also has its own experience in deciding legitimate regulatory measures. The most notable decision made in this matter was in the *Cassis de Dijon* case which stated,

‘Obstacles to movement within the community resulting from disparities between the national laws relating to the marketing of the products in question must be accepted in so far as those provisions may be recognised as being necessary in order to satisfy mandatory requirements relating in particular to the effectiveness of fiscal supervision, the protection of public health, the fairness of commercial transactions and the defence of the consumer’.<sup>35</sup>

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<sup>34</sup> A notable exception is NAFTA in Article 1114 and Article 714. Other investment treaties which contain this exception are explained in Ch.3. See also Halil Hasic, ‘Article 1110 of NAFTA: Investment Barriers to “Upward Harmonization” of Environmental Standards’ 12 (Southwestern Journal of Law and Trade in the Americas) 138.

<sup>35</sup> Case 120/78, *Rewe-Zentral AG v Bundesmonopolverwaltung für Branntwein (Cassis de Dijon)* [1979] ECR 649. Other important cases in the EU law on the matter are *Dassonville* – See Case 8/74, *Procureur de Roi v Dassonville* [1974] ECR 837 and *Keck* – See Joined Cases C-267/91 and C-268/91 *Keck and Mithouard* [1993] ECR I-6097.

The principle in the *Cassis de Dijon* case is applied throughout the EU jurisprudence, including in the area of free movement of capital and freedom of establishment as will be discussed in Chapter Four.

The past international investment cases, such as *Feldman v Mexico* suggested that the policy reasons laid by the host states which discriminate between investors must be reasonable.<sup>36</sup> Although generally the tribunals construe the reasonableness of the regulatory measures challenged, the observations made were on environmental or health issues rather than intrinsic features and problems related to investment. Apart from issues of environment and health, a research is needed to explore these areas which may include reasonable favourable treatment towards strategic investments, indigenous and infant industries,<sup>37</sup> contribution of the investment towards national security, impact of regulatory measure on rate of returns as unnecessary investment risk and deprivation of investment opportunity.<sup>38</sup>

By having a guideline of legitimate areas of governmental regulation that incorporates environmental, health, national security and issues related to investments, it will help to develop international investment law as an integrated regime, in line with other international and national concerns and with a practical international investment identity.<sup>39</sup>

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<sup>36</sup> *Feldman v Mexico*, (n 15), para 170.

<sup>37</sup> Peter Muchlinski, Federico Ortino and Christoph Schreuer, *The Oxford Handbook of International Investment Law* (1st Edition, OUP Oxford 2008) 23.

<sup>38</sup> These concerns will find its place in the concepts suggested by this thesis such as deference and proportionality in Ch.4-6 of this thesis.

<sup>39</sup> A regime that takes into account of possible areas that is “reasonable” and “legitimate” for interpretation of “likeness” as guidance for investments. For ‘integrated regime’ see also Thomas Waelde and Abba Kolo, ‘Environmental Regulation, Investment Protection and “Regulatory Taking” in International Law’ (2001) 50 *International & Comparative Law Quarterly* 811, 813.

## 2.4 Incoherence in Reference to Other Jurisprudences

The reference of past arbitration tribunals to other jurisprudences, in particular GATT/WTO has also contributed to incoherence. The incoherence arises out of the comparison to the likeness criteria in GATT/WTO as a methodology for interpretation and application.<sup>40</sup> In other words, while some tribunals referred to GATT/WTO, some others were reluctant to do so. Even where reference was made, interpretations tend to differ.<sup>41</sup> The relevance of likeness test in GATT/WTO to likeness in international investment law must be addressed before further comparisons or transposition takes place.

In *S.D Myers, Inc. v Canada* for instance, reference was made to GATT/WTO, where the determination of likeness would consider the overall GATT/WTO framework, including the general exceptions in Article XX. It suggested that likewise, national treatment under NAFTA should consider the objects and principles under the various provisions of NAFTA as well as the North American Agreement on the Environmental Cooperation (NAAEC).<sup>42</sup> The tribunal also agreed to resort to the OECD Declaration on International and Multinational Enterprises on the expression of ‘in like situations’.<sup>43</sup> In the case of *Pope & Talbot*, reference was also made to the GATT/WTO jurisprudence in discussing the general heading of NAFTA 1102.<sup>44</sup>

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<sup>40</sup> Jurgen Kurtz, ‘The Use and Abuse of WTO Law in Investor-State Arbitration: Competition and Its Discontents’ (2009) 20 *European Journal of International Law* 749.

<sup>41</sup> *Ibid.*

<sup>42</sup> *S.D Myers Inc v Canada*, (n 24), para 246.

<sup>43</sup> *Ibid.*, para 248.

<sup>44</sup> The tribunal referred to the WTO jurisprudence, i.e the cases of *Bananas and Asbestos*. See *Pope & Talbot v Canada*, (n 20) paras 50 and 58; Appellate Body Report, *European Communities –Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997,

On the other hand, the non-reference of GATT/WTO jurisprudence for the criteria of likeness was apparent in the case of *OEPC v Ecuador*. The tribunal highlighted the differences of ‘in like situation’ in investment treaties and ‘in like products’ in GATT/WTO.<sup>45</sup> *Methanex v USA* also rejected the direct use of trade law likeness test insisting that NAFTA Chapter 11 was intended for a different regime for investment than trade.<sup>46</sup> NAFTA as a treaty should be interpreted in accordance with Articles 31 and 32 of the Vienna Convention on the Law of Treaties and thus should not rely on trade criteria. Accordingly the tribunal said,

‘It may also be assumed that if the drafters of NAFTA had wanted to incorporate trade criteria in its investment chapter by engrafting a GATT-type formula, they could have produced a version of Article 1102 stating “Each Party shall accord to investors [or investments] of another Party treatment no less favorable than it accords its own investors, in like circumstances with respect to any like, directly competitive or substitutable goods”. It is clear from this constructive exercise how incongruous, indeed odd, would be the juxtaposition in a single provision dealing with investment of “like circumstances” and “any like, directly competitive or substitutable goods’.<sup>47</sup>

If the GATT/WTO jurisprudence was adopted in the case of *Methanex v USA*, the result would be different. An identical comparator who is not a direct competitor to

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DSR 1997:II, 59; Appellate Body Report, European Communities –Measures Affecting Asbestos and Asbestos-Containing Products, WT/DS135/AB/R, adopted 5 April 2001, DSR2001:V II, 3243.

<sup>45</sup> *OEPC v Ecuador*, (n 18), para 176.

<sup>46</sup> *Methanex v USA*, (n19), para 33.

<sup>47</sup> *Ibid.*, para 34.

the claimant will not be in like circumstances as compared to the ‘less’ like but direct competitor.<sup>48</sup>

### *2.5 Contribution of this Research*

The contribution of this research is to develop a doctrinal understanding of appropriate comparators in national treatment based on the underlying philosophies of international investment law and relevant criteria learnt from the GATT/WTO, EU and international human rights law. At the end of this research, it provides the criteria for the interpretation of likeness and legitimate regulatory measures in national treatment cases under investment treaties.

### **3.0 Objectives of Research**

This research undertakes the following objectives:

- i- To analyse the emerging principles in the interpretation of national treatment in international investment arbitration cases.
- ii- To analyse the relevance of the GATT/WTO, EU and the international human rights jurisprudence in the interpretation of national treatment in international investment law.

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<sup>48</sup> Methanex insisted that the GATT/WTO should be referred to. *Ibid.*, para 23.



- iii- To develop the standards in the interpretation of national treatment in international investment arbitration cases supported with the relevant GATT/WTO, EU and the international human rights jurisprudence.

#### **4.0 Research Questions**

This research seeks to address the following research questions:

- i- What are the emerging principles in the interpretation of national treatment in international investment arbitration cases?
- With whom should a claimant be compared?
  - What legitimate regulatory interest that may justify differences in treatment between foreign and domestic investor?
  - How do the emerging principles correspond with the objectives of national treatment?
- ii- How relevant are the GATT/WTO, EU and the international human rights jurisprudence in the interpretation of national treatment in international investment law?

## 5.0 Analytical Framework

This research will be guided from the viewpoint of investment security and reasonableness. These angles will provide a balanced interpretation of national treatment from the perspectives of both the host states and the investors, within the spirit of BITs, investment protections and sovereignty.<sup>49</sup>

### 5.1 Investment Security

Kenneth J. Vandevelde states that most BITs promote principally investment security.<sup>50</sup> This is related to the main rationale of concluding BITs, that is to protect covered investments from political risks. Marino Baldi described this as,

‘...to prevent countries not having sufficient tradition of applying concepts such as ‘the rule of law’ and ‘due process of law’ from taking discriminatory or arbitrary measures vis-à-vis foreigners and their property...The overall purpose of BITs-which are bilateral treaties- has never been and cannot be anything other than to provide a framework for protection against so-called political risks, namely measures that are considered to be incompatible with concepts such as ‘rule of law’ and ‘due process of law’.’<sup>51</sup>

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<sup>49</sup> The aim of BITs is to promote and protect foreign investments. See Patrick Julliard, 'Bilateral Investment Treaties in the Context of Investment Law', (Investment Compact Regional Roundtable on Bilateral Investment Treaties for the Protection and Promotion of Foreign Investment in South Europe, 2001). See also Nicholas DiMascio and Joost Pauwelyn, 'Nondiscrimination in Trade and Investment Treaties: Worlds Apart or Two Sides of the Same Coin?' (2008) 102 *The American Journal of International Law* 48.

<sup>50</sup> Vandevelde, *Bilateral Investment Treaties* (n 2) 108.

<sup>51</sup> Marino Baldi, 'Less May Be More: The Need for Moderation in International Investment Law', *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 444.

The guarantee towards favourable investment climate by promoting and protecting foreign investments is manifested in most BITs.<sup>52</sup> The national treatment provision is an important tool to encourage foreign investments bringing capital to the host countries. This explains the incorporation of non-discrimination principle that protects foreign properties in many agreements and initiatives such as the Hansaetic League,<sup>53</sup> 1929 Draft Convention,<sup>54</sup> the International Chamber of Commerce's International Code of Fair Treatment for Foreign Investment, the Abs-Shawcross Draft Convention 1959,<sup>55</sup> the Harvard Draft 1961,<sup>56</sup> the Draft OECD Convention 1967<sup>57</sup> and the 1976 OECD Declaration on International Investment and Multinational Enterprises.<sup>58</sup>

The security intended for investments is not only confined to physical security but also to functional security. Foreign investments, having sunk its capital in a foreign country is fragile and vulnerable to changes in the latter's governmental

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<sup>52</sup> Promotion and protection of investments are normally written in the preambles. See for instance Egypt-Germany BIT (2005), <[http://www.unctad.org/sections/dite/ia/docs/bits/germany\\_egypt.pdf](http://www.unctad.org/sections/dite/ia/docs/bits/germany_egypt.pdf)> accessed 9 September 2013. See also UK-Argentina BIT (1991), <[http://www.unctad.org/sections/dite/ia/docs/bits/uk\\_argentina.pdf](http://www.unctad.org/sections/dite/ia/docs/bits/uk_argentina.pdf)>, accessed on 28 January 2014.

<sup>53</sup> Rondo Cameron and Larry Neal, *A Concise Economic History of the World: From Paleolithic Times to the Present* (4th edn, OUP USA 2002).

<sup>54</sup> The Draft Convention on the Treatment of Foreigners 1929, Proceedings in League of Nations Document C.97. M.23.1930; John Ward Cutler, 'The Treatment of Foreigners: In Relation to the Draft Convention and Conference of 1929' (1933) 27 *The American Journal of International Law* 225.

<sup>55</sup> 1959 Draft Convention on Investments Abroad (Abs-Shawcross Draft Convention), International Investments: A Compendium, <<http://unctad.org/sections/dite/ia/docs/Compendium/en/137%20volume%205.pdf>>, accessed on 1 October 2013; Ignaz Seidl-Hohenveldern, 'Abs-Shawcross Draft Convention to Protect Private Foreign Investment: Comments on the Round Table, The' (1961) 10 *Journal of Public Law* 100; 'Proposed Convention to Protect Private Foreign Investment--Introduction, The' (1960) 9 *Journal of Public Law* 115; 'The Proposed Convention to Protect Private Foreign Investment - A Round Table' (2005) 2 *Transnational Dispute Management (TDM)* <<http://www.transnational-dispute-management.com/article.asp?key=458>>, accessed on 1 October 2013.

<sup>56</sup> The 1961 Draft Convention on the International Responsibility of States for Injuries to Aliens

<sup>57</sup> Draft Convention on the Protection of Foreign Property 1967, (1968) 7 *ILM* 117.

<sup>58</sup> OECD Declaration on International Investment and Multinational Enterprises, signed 21 June 1976, <<http://www.oecd.org/daf/inv/mne/50024800.pdf>>, accessed on 3 October 2013.

regulations.<sup>59</sup> The imminence of the situation is perhaps best termed as ‘obsolescing bargains’ by late Professor Raymond Vernon which was quoted in many writings to explain the weak position of foreign investors in the circumstances which force them to accept any unilateral terms imposed by the host state.<sup>60</sup> The vulnerability or exposure of risks can be from all angles of the investment, from production to labour and marketing. The exposure of risk and host states’ creativity in regulating is also mentioned in literatures<sup>61</sup> including introducing regulatory measures which are inherently discriminatory,<sup>62</sup> based on religion, language or geographical differences.<sup>63</sup> In *Mondev International Ltd v. United State of America*, the tribunal referred to the *Neer* award and commented that the international protection of foreign investment must not be confined to physical security which may be the appropriate approach in 1920s. The tribunal acknowledged that there is development by the occurrence of time. In *Mondev*:

‘Secondly, *Neer* and like arbitral awards were decided in the 1920s, when the status of the individual in international law, and the international protection of foreign investments, were far less developed than they have since come to be. In particular, both the substantive and procedural rights of the individual in international law have undergone considerable development. In the light of these developments it is unconvincing to confine the meaning of “fair and

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<sup>59</sup> One of the main risks for foreign investors is the change of rules by host states. See Jeswald Salacuse, ‘The Emerging Global Regime for Investment’ (2010) 51 *Harvard International Law* 427.

<sup>60</sup> Salacuse, *The Law of Investment Treaties* (n 4) 92; Peter D. Cameron, *International Energy Investment Law: The Pursuit of Stability* (Oxford University Press 2010) 4.

<sup>61</sup> See Anne van Aaken, ‘Perils of Success? The Case of International Investment Protection’ (2008) 9 *European Business Organization Law Review* (EBOR) 1.

<sup>62</sup> New forms of ‘taking’ are now being operated by ‘regulation’. See Waelde and Kolo, ‘Environmental Regulation, Investment Protection and “Regulatory Taking” in International Law’ (n 39) 813.

<sup>63</sup> Federico Ortino, ‘From “Non-Discrimination” to “Reasonableness”: A Paradigm Shift in International Economic Law?’ (2005). (Jean Monnet Seminar, New York University School of Law) 12.

equitable treatment” and “full protection and security” of foreign investments to what those terms – had they been current at the time – might have meant in the 1920s when applied to the physical security of an alien. To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith.’<sup>64</sup>

Investment security requires host state to allow foreign investors fair competition in the market; ensuring level playing field. Distortion of the market would amount to changes contrary to the investors’ legitimate expectation. The national treatment provision is expected to serve as an effective mechanism to hinder host states from introducing protectionist measures and discriminatory treatments.

In construing the needs of investments, it should be assumed that all investments require a neutral, if not friendly investment atmosphere. Investments should be able to operate in the ordinary course of business without procedural complications which may cost time and expenses. Loss of time and expenses would eventually lead to loss of competitiveness and returns. Foreign investments therefore also strive to compete for the soft or smooth procedures or laws to ensure that the ‘establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments’ would be the same as provided for to the domestic investors.

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<sup>64</sup> *Mondev International Ltd v. United State of America* (2002) ARB (AF)/99/2 para 116. See also *Compania de Aguas del Aconquija S.A and Vivendi Universal S.A v Argentine Republic*, Award, ICSID Case No. ARB/97/3, 20 August 2007, para 7.4.7, page 202 and *CME Czech Republic B.V (The Netherlands) v The Czech Republic, Final Award, UNCITRAL*, 14 March 2003, para 499.

Not only do the foreign investors need investment security, the host states also need the same. Foreign investments bring various advantages to the host states, among which are the creation of new jobs, development of natural resources, transfer of skill and technology, improved linkages with the world markets and improvement of balance of payments.<sup>65</sup> It is also in the interest of the host states to maintain the investors in the state as a sign of stability and honouring the commitments in the investment agreements which would further attract more investors.

### *5.3 Reasonableness*

In determining appropriate comparators, two investors/ investments can be considered unlike if there is justification or reasonableness for the discriminatory measure. The criteria for the appropriate comparator therefore must be based on this ground. Looking at national treatment from the viewpoint of reasonableness provides a balanced approach as it gives room to the host state to exercise its sovereignty to introduce regulatory measures as long as they are legitimate.

Within international investment law, Kenneth J. Vandewelde puts reasonableness as one of the core principles of the BITs.<sup>66</sup> The investment tribunals have resorted to

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<sup>65</sup> The need for investment has encouraged countries to sign BITs. See Zachary Elkins, Andrew T Guzman and Beth A Simmons, 'Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000' [2006] International Organization 811. and Andrew T Guzman, 'Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties' (1998) 38 Virginia Journal of International Law 639.

<sup>66</sup> Other core principles are access, security, non-discrimination, transparency and due process. See Vandewelde, *Bilateral Investment Treaties* (n 2) 2. In relation to this, Marino Baldi emphasised that the aim of investment treaties is to protect investments. He disagreed with attempts to stretch the use of BITs for the furtherance of other purposes, such as claims for large amounts of compensation for damages caused by measures of general application dealing with public health or environment. His article is in line with the rationale of forwarding the principle of 'reasonableness' as the second tier

general public international law principles to interpret the broad provisions of the BITs, which may enhance the protection on foreign investors.<sup>67</sup> Reasonableness is among other general principles referred to (such as proportionality, transparency and due process), but it is more common in fair and equitable treatment.<sup>68</sup> The quest towards reasonable results of investment decisions is in line with Article 32(b) of the VCLT. The tribunals could set aside interpretations which would lead to ‘a result which is manifestly absurd or unreasonable. It also brings the interpretation closer to the context, promotes teleological construction of the subject matter of dispute and lead towards a more ‘legislator-oriented’ decisions.<sup>69</sup>

The move towards reasonableness is also forwarded by Professor Andreas F. Lowenfeld highlighting that there is a trend in favour of the reasonableness principle across numerous international litigations.<sup>70</sup> In national treatment, the principle of reasonableness is applied but with less emphasis which perhaps spurred Federico Ortino’s work urging to move towards reasonableness. This work provides insight to view reasonableness from the investors’ point of view, by applying the reasonableness related tests of necessity, proportionality, transparency and participation.<sup>71</sup>

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of the analytical framework of this thesis, in order to achieve a balanced interpretation. See Baldi, ‘Less May be More: the Need for Moderation in International Investment Law’ (n 51).

<sup>67</sup> Jurgen Bering and others, ‘General Public International Law and International Investment Law: A Research Sketch on Selected Issues’ (The International Law Assoc. German Branch Sub-Committee on Investment Law) 23 < <http://telc.jura.uni-halle.de/sites/default/files/BeitraegeTWR/Heft%20105.pdf> >, accessed on 28 January 2014.

<sup>68</sup> *Pope & Talbot Inc. v Canada*, (n 20), para 123.

<sup>69</sup> Ole Kristian Fauchald, ‘The Legal Reasoning of ICSID Tribunals – An Empirical Analysis’ (2008) 19 *European Journal of International Law* 301.

<sup>70</sup> Andreas F Lowenfeld, ‘Investment Agreements and International Law’ (2003) 42 *Columbia Journal of Transnational Law* 123, 231.

<sup>71</sup> Ortino, ‘From “Non-Discrimination” to “Reasonableness”: A Paradigm Shift in International Economic Law?’ (n 63).

This research will portray how reasonableness interacts with investment security and what effect they will bring to the determination of appropriate comparator. Although investors dislike abrupt changes, or changes at all affecting their investments, host states nevertheless have certain discretion to change policies. Here, the principle of reasonableness comes into play. In light of reasonableness of government regulatory measures, this analysis will also examine whether competition benefited from liberalisation should be given an exclusive or a non-exclusive approach in considering comparability between the investors and domestic investors.

## **6.0 Significance of Research**

### *6.1 Coherence in National Treatment*

This research addresses and provides suggestions towards coherence in the level of protection that investors could rely on under the national treatment principle. Even though the arbitrators are not bound by the doctrine of judicial precedence, it is necessary to increase predictability,<sup>72</sup> maintain and enhance credibility of this area of law.<sup>73</sup> Salacuse has highlighted that the 3000 international investment treaties concluded has already constituted an emerging global regime for investment.<sup>74</sup> As a regime, coherence is no longer an option, but necessary to allow it to evolve as a credible jurisprudence. In this matter, Reinisch mentioned,

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<sup>72</sup> Andrea K. Bjorklund, 'Investment Treaty Arbitral Decisions as Jurisprudence Constante' [2008] UC Davis Legal Studies Research Paper, also in Colin B Picker, Isabella D Bunn and Douglas W Arner (eds), *International Economic Law: The State and Future of the Discipline* (Hart Publishing, 2008) 266.

<sup>73</sup> See Gabrielle Kaufmann-Kohler, 'Arbitral Precedent: Dream, Necessity or Excuse? The 2006 Freshfield Lecture. See also Jeffery P. Commission, 'Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence' (2007) 24(2) (*Journal of International Arbitration*) 129-158.

<sup>74</sup> Salacuse, 'The Emerging Global Regime for Investment' (n 59).



‘It is immediately apparent that this kind of lack of coherence may seriously diminish the appeal of investment arbitration because it will decrease the confidence of potential claimants, as well as respondents, in a predictable form of dispute settlement.’<sup>75</sup>

Andrea K Bjorklund has also foreseen the practical problems if the decisions are not consistent- among which is - with the increase number of conflicting cases, it will soon be difficult for arbitrators themselves to canvass all relevant prior cases.<sup>76</sup> Conflicting decisions in arbitration awards constitute a cause of incoherence and inconsistency in international investment law.<sup>77</sup>

Having identified the issue of likeness which constitutes the biggest inconsistency in national treatment, it is necessary to maximise its potential towards predictability by filling in the gap in creating guidelines on the interpretation of likeness and legitimate regulatory measures based on previous investment cases and expanding references to other relevant jurisprudence of earlier experience.<sup>78</sup> It is pertinent to this thesis that the coherence sought is not ‘consistency for consistency’s sake’ but an effort towards predictability of quality interpretations that take into account the

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<sup>75</sup> August Reinisch, ‘The Challenge of Fostering Greater Coherence in International Investment Law’ in Roberto Echandi (ed), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 236.

<sup>76</sup> Bjorklund, ‘Investment Treaty Arbitral Decisions as Jurisprudence Constante’ (n 72).

<sup>77</sup> This is in addition to the fragmented legal foundation in the large number of BITs and the increasing regional and multilateral treaties. See Christoph Schreuer, ‘Coherence and Consistency in International Investment Law’ in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 391, 398.

<sup>78</sup> Andrea K Bjorklund claims that to achieve persuasion, precedent and jurisprudence *constante*, it is necessary to examine how to treat the decisions to maximize their potential for creating predictability and widely accepted principles of investment law. See Bjorklund, ‘Investment Treaty Arbitral Decisions as Jurisprudence Constante’ (n 72) 270.

context and underlying philosophies of national treatment and investment treaties.<sup>79</sup>

It works for coherence within the current setting of investment treaties by way of interpretation.<sup>80</sup>

Should there be coherence in the understanding of national treatment provisions, it will help both the host states and the investors to minimise disputes which are both expensive and time consuming.<sup>81</sup> Certainty in law thus brings respect towards international investment law, in line with the spirit of *pacta sunt servanda* where treaties are based on.

## 6.2 Better Investment Climate

This research responds to the concerns faced by investors against discrimination and unfair level playing field.<sup>82</sup> Discrimination in the form of national treatment has increasingly becomes a barrier replacing expropriation. This is due to the shift towards regulatory state where the investors' position becomes more exposed to

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<sup>79</sup> Michael Ewing-Chow has raised this provocative idea of consistency. This is a useful observation which should encourage caution in the direction of consistency that is often promoted in international investment law. See World Trade Forum and Michael Ewing-Chow, 'Coherence, Convergence and Consistency in International Investment Law' in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 232.

<sup>80</sup> Rudolf Dolzer highlighted three lines of argument in relation to consistency in international investment arbitration, i.e embracing the status quo, a call for serious overhaul and improving the current regime. This thesis works in line with the third argument. See Rudolf Dolzer, 'Perspectives for Investment Arbitration: Consistency as a Policy Goal?' in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 409.

<sup>81</sup> The ICSID Caseload Statistics. Issue 2010-1. Chart 1: Total Number of ICSID Cases Registered by Year.

<<http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=ShowDocument&CaseLoadStatistics=True&language=English>>7, accessed on 28 January 2014.

<sup>82</sup> Marcin Sobczyk, 'Foreign Investors Allege Discrimination in Hungary' *The Wall Street Journal* (January 3, 2011) <<http://blogs.wsj.com/new-europe/2011/01/03/foreign-investors-allege-discrimination-in-hungary/>> accessed on 28 January 2014.

discriminatory measures by way of regulatory conducts and administrative practice.<sup>83</sup> As domestic politics are unpredictable, there appears to be a need of external disciplines in order to create good governance and investment climate.

The outcome of this situation is not difficult to see as although investment cases on national treatment grew only in the 2000s, it has become an area of speculation among the investment players, be it the investors, the host states and even the legal academia. The incoherence of the interpretation of national treatment principle had caused parties to be at a limbo, as there is no predictable set of legal explanations that they could rely on not only when disputes are already filed in an arbitration tribunal, but during the day to day business. Host states may end up facing million dollars' worth of suit under national treatment because of mistakes in actions or regulations.

A good investment climate means consistent and predictable investment regulations. It is impossible for states and investors to contemplate matters within their rights if there is no guide in the interpretation of national treatment. As a comparison, expropriation has its own standards developed in some BITs, cases and literatures which make it more certain.<sup>84</sup> As a result of inconsistencies, foreign investors have the tendency to abandon even the most profitable investment opportunity if they think that the investment climate is threatening.<sup>85</sup>

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<sup>83</sup> Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

<sup>84</sup> Waelde and Kolo, 'Environmental Regulation, Investment Protection and "Regulatory Taking" in International Law' (n 39) 826–827. See also 2004 US Model BIT, Article 6 <<http://www.state.gov/documents/organization/117601.pdf>>, accessed on 28 January 2014.

<sup>85</sup> Ibrahim F. Shihata, 'Encouraging International Corporate Investment: The Role of The Multilateral Investment Guarantee Agency' (1998) 23 Columbia Journal of World Business 11.

## 7.0 Research Methodology

This research is a qualitative study, applying the doctrinal legal research and comparative research approach. It involves textual studies of national treatment provisions from the relevant BITs and other international investment agreements, arbitration awards and scholarly interpretations in the legal academia. The similar contents of national treatment provisions in BITs provide a considerable source of reference within international investment law. Such, in a wider context, has even been regarded as the emergence of a new ‘customary international law’ by Andreas F. Lowenfeld and as a ‘regime’ by Jeswald Salacuse, suitable for doctrinal analysis.<sup>86</sup> Doctrinal analysis is deployed to examine the content of the legal contents and opinions and to analyse the reasoning.<sup>87</sup> Accompanied with the doctrinal analysis, this research will also apply the comparative approach which is another common method in legal studies. The basic methodological principle in the recent legal comparative analysis is the ‘principle of functionality’ which allows jurisprudences to benefit from each other the tools of interpretation in comparable areas of research.<sup>88</sup> Below are the explanations of the methodology used in the context of this research:

### *7.1 Doctrinal and Comparative Legal Research*

The doctrines which are the subjects of research are primarily the national treatment provisions and the non-discrimination principles in the international investment law,

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<sup>86</sup> Lowenfeld, ‘Investment Agreements and International Law’ (n 70); Salacuse, ‘The Emerging Global Regime for Investment’ (n 59).

<sup>87</sup> Emerson H. Tiller and Frank B. Cross, ‘What is Legal Doctrine’ (2006) Northwestern University Law Review.

<sup>88</sup> Ralf Michaels, ‘The Functional Method of Comparative Law’ in Mathias Reimann and Reinhard Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP Oxford 2008); Christopher A Whytock, ‘Legal Origins, Functionalism, and the Future of Comparative Law’ (2009) 6 Brigham Young University Law Review.

the GATT/ WTO, the EU and the international human rights law. This research studies the common elements in the jurisprudences in relation to national treatment and the non-discrimination principle in the investment context. It analyses whether there are lessons from GATT/ WTO, the EU and the international human rights jurisprudences that could be learned by international investment law. It builds the criteria for likeness and legitimate regulatory measures in the perspective of national treatment in line with the doctrinal and comparative legal research it conducts. The scope of doctrinal and comparative legal research in the jurisprudences is as the following:

#### *7.1.1 National Treatment in GATT/WTO*

Under the WTO law, the main area of doctrinal analysis and comparison is Article III of the General Agreement on Tariffs and Trade (GATT). The GATT/WTO provides for national treatment obligations on internal taxes, charges and regulatory measures affecting the sale of products.<sup>89</sup> The GATT/WTO panels have confronted the issue of like products in their cases. The criteria that are applied to establish likeness are the competitiveness test based on the products' end-users in a given market, consumers' tastes and habits, the products' property, nature and quality, the products' tariff classification and the aim and effect test. This research examines how the panels construe the criteria in the cases and how it may be relevant to international investment cases.

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<sup>89</sup> Article III:2-4 GATT 1947.

### 7.1.2 Non-Discrimination Based on Nationality in EU Law

The two important areas of the EU law which are the subject of comparison are free movement of capital 63(1) TFEU (ex Article 56 TEC) and freedom of establishment Article 49 TFEU (ex Article 43 TEC). Freedom of investment, although not explicitly referred by the term, is covered in the two freedoms mentioned.<sup>90</sup> By virtue of these freedoms, non-nationals from a member state are allowed to establish their investments and freely move their capitals without discrimination and restriction.<sup>91</sup>

Discrimination on the basis of nationality may occur in investments by way of direct taxation (income and incorporate taxes).<sup>92</sup> The member states still preserve their sovereign power to subject investments to certain requirements or regulations. This national control however must respect the fundamental freedoms provided for in the EU law. Case laws have been brought by the EU to challenge member states' discriminatory regulations.<sup>93</sup> This comparative method will analyse the issue of likeness in investments, unreasonable and reasonable regulatory measures in the EU jurisprudence.

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<sup>90</sup> Freedom of investment is often subjected to many definitions. Common concepts of freedom of establishment and free movement of capital are reverted to when dealing with investment. For further discussion, see P Juillard, 'Freedom of Establishment, Freedom of Capital Movements, and Freedom of Investment' (2000) 15 ICSID Review 322.

<sup>91</sup> In the interpretation of these freedoms, along with other freedoms in the EU law, the principle of equal treatment is applied as a common thread. See Michel Aujan, 'The Future of Non-Discrimination – Direct Taxation in Community Law' in Reuven Avi-Yonah, James Hines and Michael Lang (eds), *Comparative Fiscal Federalism: Comparing the European Court of Justice and the US Supreme Court's Tax Jurisprudence* (Kluwer Law International 2007) 322.

<sup>92</sup> As compared to indirect taxation which is harmonised in almost every issue, there are a few areas which are harmonised in direct taxation, such as Merger Directive 90/434/EEC, the Parent-Subsidiary Directive 90/435/EEC and the Arbitration Convention 90/436/EEC.

<sup>93</sup> See Case C-324/00 *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt*, 2002 E.C.R I-11779, Case C-168/01 *Bosal Holding BV v. Staatssecretaris Van Financiën*, 2003 E.C.R I-9409.

### *7.1.3 Non-Discrimination Principle in the International Human Rights Law*

The main examination involved in this thesis is the European Convention of Human Rights (ECHR) in particular, Article 1 Protocol 1 (A1P1) on the right to property taken together with Article 14 which prohibits discrimination. The effect of these provisions is that they provide a similar form of protection as the national treatment provision. Investors and businesses have increasingly resorted to these provisions against discriminatory measures by the member states.<sup>94</sup> Cases brought under these provisions have decided on comparability issues and legitimate regulatory measures. Scholarly articles have also highlighted the importance of the issue of determining comparators in discrimination cases which are a fertile area of research for this thesis.<sup>95</sup>

### *7.1.4 Relevance of Comparison with GATT/WTO, EU and International Human Rights*

The study of the GATT/ WTO, the EU, the international human rights jurisprudence and the various investment treaties (NAFTA, Energy Charter Treaty, BITs) is undertaken based on the possible common economic philosophy of liberalisation, protection of property rights and non-discrimination.<sup>96</sup>

It analyses the application of the non-discrimination principle and its role in the bigger objectives of the treaties including economic integration and creating a level

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<sup>94</sup> Further explanation on reference to the international human rights law is dealt in Ch. 5.

<sup>95</sup> Aileen McColgan, 'Cracking the Comparator Problem: Discrimination, Equal Treatment and the Role of Comparisons' (2006) 6 European Human Rights Law Review 650; Issac Joory, 'Arguments Against the Politicized Role of Comparators in Article 14 Discrimination Cases' (2009) 5 Cambridge Student Law Review 40.

<sup>96</sup> Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

playing field in a competitive market economy. This is achieved by studying the philosophies of these jurisprudences in their evolution which involves the political economy and the circumstances of the post-World War II development in trade and investments. Compatibility will be determined based on the commonalities reached among the jurisprudence as compared to international investment law.

Reference to the GATT/WTO, the EU and the international human rights jurisprudence is conducted on the basis that they may assist in the interpretations of the non-discrimination principle. All three jurisprudences ask the same questions in construing discrimination cases (i.e the determination of comparators and objectivity of justifications) and involve cases against state measures. They have relatively earlier experience and an extensive number of case laws. These jurisprudences contain protections on foreign investors or traders against regulations which discriminates domestic players. There is therefore a basis to systematically study and seek the commonalities that may benefit international investment law.

It is observed that the reference to the EU law is less undertaken. Similarly, the international human rights law is not found discussed in the context of national treatment in investment cases.<sup>97</sup> The comparison so far has only actively been with GATT/WTO.<sup>98</sup>

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<sup>97</sup> In terms academic discussion, there is an attempt of this nature by Freya Baetens, 'Discrimination on the Basis of Nationality: Determining Likeness in Human Rights and Investment Law' in Stephen W.Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press 2010).

<sup>98</sup> See generally *Methanex v USA*, (n 19), *SD Myers, Inc. v Canada*, (n 24) and *Corn Products International, Inc v The United Mexican States* ICSID Case No ARB (AF)/04/01, Decision on Responsibility, 15 January 2008 (hereinafter '*CPI, Inc. Mexico*').



This research also serves to respond to the cries towards convergence in international economic law, to point a few - as a notion of a possible emergence of common law in international economic law,<sup>99</sup> comparative method as an indispensable tool for the construction of the ‘science’ of international economic law<sup>100</sup> and as a period of convergence in international economic law<sup>101</sup> - to the extent of analysing the possible areas that jurisprudences may benefit from each other. Although there are different textual wordings in the jurisprudences, the economic logic is similar.<sup>102</sup> The three jurisprudences contribute to liberalisation of trade and investment, state-to state exchanges of market access and trade and investment opportunities.<sup>103</sup>

This research revolves around the common minimum standard of non-discrimination principle, which exists in all the three jurisprudences. The standard on non-discrimination principle will help to answer the research question by identifying the emerging principles in likeness in discrimination tests, the purpose and intention of national treatment and justifications of discriminatory treatments. Interaction therefore is plausible due to the common language and the same industrial players (especially in trade and investments) – the lawyers, arbitration panels and drafting committee and the same general aim of the national treatment protection.

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<sup>99</sup> JHH Weiler, ‘Cain and Abel- Convergence and Divergence in International Trade Law’ in *The EU, the WTO and the NAFTA: Towards a Common Law of International Trade?* (OUP, Oxford 2000) 1.

<sup>100</sup> Federico Ortino, *Basic Legal Instruments for the Liberalisation of Trade: A Comparative Analysis of EC and WTO Law* (Hart Publishing, North America 2004) 5.

<sup>101</sup> Todd Weiler, ‘Saving Oscar Chin: Non-Discrimination in International Investment Law’, *International Investment Law and Arbitration: Leading Cases from ICSID, NAFTA, Bilateral Treaties and Customary International Law* (Cameron May, London 2005) 559.

<sup>102</sup> Jurgen Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’ in Stephen W. Schill (ed) *International Investment Law and Comparative Public Law* (OUP, UK 2010) 243.

<sup>103</sup> In the context of international trade law and international investment law, see DiMascio and Pauwelyn, ‘Nondiscrimination in Trade and Investment Treaties’ (n 49).

This study is of importance to the whole development of international investment law, not confining itself to ICSID or NAFTA disputes. The *fora* of arbitration, being left at the liberty of the disputing parties, may lead them to resort to non-institutional tribunals (ad hoc tribunals), or being guided only by UNCITRAL rules, which opens the application of other related jurisprudences outside international investment law. Thus, interaction with other jurisprudences is necessary to understand the commonality and the differences which may be applicable at hand.

## *7.2 Sources of Research*

This research refers mostly bilateral and multilateral investment treaties, relevant international conventions, textbooks, case reports and journal articles in the form of printed, visual, digital and any other retrievable format. It also includes the utilisation of online databases, among others Transnational Dispute Management (TDM), LexisNexis, HeinOnline and Westlaw International, Kluwer Arbitration, Investor-State Law Guide, ICSID, UNCTAD, Eur-Lex Access to European Union Law, HUDOC European Court of Human Rights and WTO websites and databases. In carrying out this method of research, focus is given to published academic discussions on the subject matter to preserve the objectivity and reliability of this research.

## **8.0 Thesis Structure**

This research consists of six chapters. The first chapter outlines the foundation of the thesis, which includes the problem statement, research question, object, methodology, literature review, analytical framework and significance of the research.

The second chapter underlines the doctrinal evolution of the national treatment principle in the history. It also explains the scope of national treatment in different investment treaties and put the application of national treatment in treaty practice into perspective. It elaborates the interpretative problems of national treatment which are the focus of this thesis, i.e how the tribunals have interpreted likeness and determine legitimate regulatory measures. It triggers the relevant questions and provides the general status quo of the jurisprudence for the comparative exercise in the subsequent chapters that follow.

The third chapter discusses the most controversial question of relevance of other jurisprudence in national treatment as presented in investment arbitrations. The GATT/WTO has always been the shadow jurisprudence behind an international investment law national treatment interpretation. The relevance or plausibility of referring to it is however debatable. Yet, there are potential interpretative mechanisms that may be helpful to investment law considering the similar question posed in both jurisprudences. This chapter thus firstly explores the plausibility of reference and proceeds to find the lessons that could be learnt from this jurisprudence.

The fourth chapter is an attempt to seek the relevance of the European Union law to investment treaties specifically from the viewpoint of two freedoms i.e freedom of establishment and free movement of capital. This chapter examines the philosophy of the EU law and the analogous effect of national treatment in the two freedoms. It proceeds with the analysis of likeness and observations on the similarity and difference of level of integration and their relevance to the determination of legitimate regulatory measures.

The fifth chapter focusses on the relevance of international human rights law. It highlights the similarity in the non-discrimination principle as protection of investors'/investments' property. It examines the ECHR approach in determining discrimination cases including the methodology of assessment of likeness and the application of relevant administrative principles.

The final chapter is a thorough synthesis on the lessons taken from the jurisprudences under comparison. It incorporates these lessons into the investment context by analysing and revisiting investment cases. It suggests the extent of suitability and develops the criteria of likeness to be applied in the investment disputes. It also attempts to relate the thesis with the analytical framework and the significance of the research as proposed in this chapter.

## 9.0 Literature Review

Literatures on the determination of likeness in international investment law are generally not found as standing on their own. It is mostly discussed under the headings of national treatment or non-discrimination as part of examining the required thresholds of national treatment. Among the prominent investment law writers whom have elaborated to a certain extent on likeness in national treatment chapters are Rudolf Dolzer and Christoph Schreuer, Newcombe, Vandevelde<sup>104</sup> Baeten and Bjorklund.A.K..<sup>104</sup> Earlier works by prominent scholars can be found written for seminars in response to earlier NAFTA disputes, among which are by Walde,<sup>105</sup> Dolzer<sup>106</sup> and Rojas F.G.<sup>107</sup>

This current research was triggered by the observation made in Dolzer that the case laws of national treatment failed to address the inconsistency in the definition of ‘business’ and ‘sector’ for the purpose of comparison in national treatment, hence resulted to the inconsistency in the interpretation of likeness.<sup>108</sup> Newcombe also highlighted the complexity of equating circumstances with operating in the same sector of the economy. The same was observed by Vandevelde claiming that some

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<sup>104</sup> Dolzer and Schreuer, *Principles of International Investment Law* (n 27); Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7); Vandevelde, *Bilateral Investment Treaties* (n 2); Andrea K Bjorklund, ‘National Treatment’ in August Reinisch (ed), *Standards of Investment Protection* (Oxford University Press 2008). August Reinisch, *Standards of Investment Protection* (OUP, UK 2008); Freya Baetens, ‘Discrimination on the Basis of Nationality: Determining Likeness in Human Rights and Investment Law’ (n 97).

<sup>105</sup> Walde, ‘Comments on the Discipline of ‘National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3).

<sup>106</sup> Part of this paper appeared in his later book ‘Principles of International Investment Law’. See Rudolf Dolzer, ‘National Treatment: New Developments’ (Symposium Co-Organised by ICSID, OECD and UNCTAD - Making the Most of International Investment Agreements: A Common Agenda. OECD Headquarters Paris).

<sup>107</sup> Fernando Gonzales Rojas, ‘The Notion of Discrimination in Article 1102 of NAFTA’ [2005] Jean Monnet Seminar: Advanced Research in the Law and Policy of the EU, NAFTA and WTO, New York University School of Law.

<sup>108</sup> Dolzer and Schreuer, *Principles of International Investment Law* (n 27).

investments may not be identical but operate overlapping tasks. He examined ‘in like circumstances’ in the view that investments must be in the same economic sector.<sup>109</sup>

In an article by Todd Weiler, it highlighted the case of *Loewen Group, Inc. and Raymond L. Loewen v. United States of America* as departing from the earlier approach in *Pope & Talbot v Canada*, *Feldman v Mexico* and *SD Myers v Canada*, as adopting “likeness simpliciter” that investments should be in the same sector.<sup>110</sup>

Bishop R.D *et al* in their commentaries, pointed at the possibility that agreements can be reached on what is “like” circumstances, but agreed that such is not an easy practice referring to the experience of the GATT/WTO.<sup>111</sup> Subedi stated that what are and are not like circumstances is often a matter of controversy.<sup>112</sup> Extensive discussions were however not made on the matter in any of the writings.

It is observed that the literatures, like the panels in arbitrations, prefer to leave the matter of likeness to be determined on a case by case basis. Vandevelde went further to conclude that a national treatment claim should be found violated if there was a discriminatory motive and if there was no legitimate host-state regulatory interest, even in the absence of a plausible comparator.<sup>113</sup> This approach seems to suggest that the determination of appropriate comparator finds less importance in the invocation of a national treatment violation. This research disagrees on such approach as the insertion of ‘in like circumstances’ or ‘situation’ is not without purpose, and should

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<sup>109</sup> Vandevelde, *Bilateral Investment Treaties* (n 2) 385.

<sup>110</sup> Todd Weiler, ‘Saving Oscar Chin: Non-Discrimination in International Investment Law’ in Todd Weiler (ed), *International Investment Law and Arbitration: Leading Cases from the ICSID, NAFTA, Bilateral Treaties and Customary International Law* (Cameron May 2005) 569. ; *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, 26 June 2003 (hereinafter ‘Loewen Case’); *Pope & Talbot v Canada*, (n20), *Feldman v Mexico*, (n15) and *SD Myers v Canada*, (n 24).

<sup>111</sup> R. Doak Bishop, James Crawford and W. Micheal Reisman , *Foreign Investment Disputes: Cases, Materials and Commentary* (Kluwer Law International, Netherland 2005) 1154.

<sup>112</sup> Subedi, *International Investment Law: Reconciling Policy and Principle* (n 27) 101.

<sup>113</sup> Vandevelde, *Bilateral Investment Treaties* (n 2) 385.

be used as the test to invoke difference of treatment between the local and foreign investors before moving on or simultaneously with the reasonableness of the measure. Even in the absence of the phrase ‘in like circumstances’ in the treaty, it is common sense to determine a discrimination claim to compare between like and like.<sup>114</sup> This also creates a line between a claim under national treatment and a claim under the fair and equitable treatment provision. The view of Newcombe perhaps is a better approach as compared to Vandevelde which chose to shift to find the legitimacy or reasonableness of the discriminatory measure taken by the host state. Newcombe claimed that the like circumstances analysis cannot be divorced from the reasons for the treatment in question. In the context of NAFTA, Rojas has made an observation on how the tribunals have resorted to the assessment of likeness in order to avoid the question of intent. On the flipside of this observation, this thesis aims to pull tribunals from such avoidance and attempt to cast the role of intent or protectionist intent to the assessment of like circumstances.<sup>115</sup>

National treatment has invited comparative studies with the WTO either by scholars of international trade or international investment. Such studies have been sparked by the reference of international investment arbitrations to the WTO jurisprudence. The study of national treatment in investment treaties and its connectivity to protectionism is a major concern in articles by Kurtz.<sup>116</sup> He contended that the correct approach of interpreting national treatment in investment treaties is to put that obligation as a constraint against protectionism. This suggestion seemed to stem

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<sup>114</sup> Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 161.

<sup>115</sup> Rojas, ‘The Notion of Discrimination in Article 1102 of NAFTA’ (n 107).

<sup>116</sup> Jorgen Kurtz, ‘National Treatment, Foreign Investment and Regulatory Autonomy: The Search for Protectionism or Something More?’ P. Kahn, T. Walde (ed), *New Aspects of International Investment Law* (2007) 311-351.

out of the debate that the interpretation of national treatment in investment treaties should not rely on GATT/WTO mainly based on several stark contextual differences between the two jurisprudence, namely the absence of GATT III:1, the GATT Article XX equivalent, and the right of private investors in bringing direct arbitral proceedings in most investment treaties. The article suggested that the protectionist approach will further raise an interpretative task to determine what will constitute protectionism, which will hence be undertaken by this research in relation to competition and discrimination.

In another article by Kurtz,<sup>117</sup> a firmer argument was brought forward claiming that the misuse of WTO law contributed to the inconsistency in the international investment law jurisprudence. Kurtz recognised that there is a problem in the transposition of WTO law wrongly in international investment disputes, *OEPC v Ecuador* being the most criticised in the article. A departure from this literature is perhaps to analyse the jurisprudences, should there be possible ways to correctly transpose the WTO law in areas of similarities into international investment disputes. Kurtz's later article reinforced his earlier stand on the transposition of WTO law in international investment arbitrations.<sup>118</sup> This thesis expands the discussions put forth in Kurtz's articles in the GATT/WTO context and extends the comparative study on likeness with the EU and international human rights jurisprudence.

Walde observed that despite some differences, there is an increasing proximity and reason for partial convergence between the WTO and international investment

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<sup>117</sup> Kurtz, 'The Use and Abuse of WTO Law in Investor-State Arbitration' (n 40).

<sup>118</sup> Jurgen Kurtz, 'The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO' in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press 2010) 243.



treaties. His article was projected on the claim that national treatment is a capable mechanism of an external discipline to promote good governance of the global economy.<sup>119</sup> The article triggers this current research in the sense that there is a ground of comparative study between national treatment in investment treaties, the WTO and the EU. DiMascio and Pauwelyn also outlined the common roots of WTO and investment law and the possible interaction between them.<sup>120</sup>

Gaeten. V. observed that the application of WTO principles as an interpretative tool is possible in disputes relating to BITs. He mentioned that the relevant provisions of the WTO are likely to pave way for international law standards of treatment to be applied in investment cases. In the alternative, even if the WTO law could not be construed as applicable to the investment disputes, it may still contribute as an ‘interpretative context’, pursuant to Article 31 (3)(c) of the Vienna Convention on the Law of Treaties.<sup>121</sup> Scholarly articles on GATT/WTO are also referred to in conducting this research. Among them are those by Horn and Mavroidis,<sup>122</sup> Hudec<sup>123</sup> and Mark Liang.<sup>124</sup>

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<sup>119</sup> Walde, ‘Comments on the Discipline of National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3).

<sup>120</sup> DiMascio and Pauwelyn, ‘Nondiscrimination in Trade and Investment Treaties’ (n 49).

<sup>121</sup> Gaetan Verhoosel, ‘The Use of Investor–State Arbitration Under Bilateral Investment Treaties to Seek Relief for Breaches of WTO Law’ (2003) 6 *Journal of International Economic Law* 493.

<sup>122</sup> Henrik Horn and Petros C. Mavroidis, ‘Still Hazy after All These Years: The Interpretation of National Treatment in the GATT/WTO Case-Law on Tax Discrimination’ (2004) 15 39.

<sup>123</sup> Robert E. Hudec, ‘GATT/WTO Constraints on National Regulation: Requiem for an “Aim and Effects” Test’ (1998) 32 *The International Lawyer* 623; Robert E. Hudec, “‘Like Product’: The Differences in Meaning in GATT Articles I and III’ in Thomas Cottier and Petros Constantinos Mavroidis (eds), *Regulatory Barriers and the Principle of Non-discrimination in World Trade Law: Past, Present, and Future* (University of Michigan Press 2000).

<sup>124</sup> Mark Liang, ‘Green Taxes and the WTO: Creating Certainty for the Future’ (2009) 10 *Chicago Journal of International Law* 359.

Direct studies comparing international investment law, GATT/WTO and the EU jurisprudence are rare in the context of the interpretation of likeness in national treatment. Studies however can be found comparing international investment law and WTO as a pair (as noted a few in the above literatures) or WTO and the EU as another pair.<sup>125</sup> An example is the comprehensive comparative study by Ortino, which compares the WTO and the EU in the view of non-discrimination.<sup>126</sup>

In the reading from the EU perspective, Steffen Hindelang has made a connection between free movement of capital and freedom of establishment in the EU law with national treatment in international economic law. Both Articles 49 (ex Article 43 EC) and Art 56 EC (now A63 TFEU) include a prohibition of discrimination. In both cases, if cross-border and domestic situations are compared, they correspond to the international economic law principle of national treatment.<sup>127</sup> Another important scholarship in the field is Tom O'Shea who has contributed significantly in tax areas involving freedom of establishment and free movement of capital.<sup>128</sup> His writings have casted insights to the comparative exercise in this thesis.

Juillard, P had attempted to discuss the relationship between the freedoms; freedom of establishment, freedom of movement and freedom of investment. He contended

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<sup>125</sup> G De Búrca and Joanne Scott, *The EU and the WTO: Legal and Constitutional Issues* (Hart Pub. 2001).

<sup>126</sup> Federico Ortino, *Basic Legal Instruments for the Liberalisation of Trade: A Comparative Analysis of EC and WTO Law* (Hart Publishing 2004).

<sup>127</sup> Steffen Hindelang, *The Free Movement of Capital and Foreign Direct Investment: The Scope of Protection in EU Law* (OUP Oxford 2009) 129–135.

<sup>128</sup> Tom O'Shea, 'Freedom of Establishment Tax Jurisprudence: Avoir Fiscal Re-visited' (2008) 6 Tax Review, <<http://www.ccls.qmul.ac.uk/docs/staff/oshea/52178.pdf>>, accessed on 14 October 2013; Tom O'Shea, 'Taxation of Non-Residents' [2009] *The Tax Journal* <<http://www.ccls.qmul.ac.uk/docs/staff/oshea/52213.pdf>> accessed 28 January 2014; Tom O'Shea, 'Truck Center: A Lesson in Source Vs. Residence Obligations in the EU' (2009) 53 Tax Notes International 593.

that due to the multiplicity of definitions of the term investment, the term freedom of investment has not gained significant acceptance.<sup>129</sup>

Aujean, M. observed that challenges of direct taxations will continue and that it is likely that it will induce collective action by the member states to ensure coherence at the community level.<sup>130</sup> This article also shed some light on a number of justifications for discriminatory measures by member states from decided cases.

As far as the principle of reasonableness is concerned, Ortino has explored the relationship between reasonableness and national treatment comparing WTO and NAFTA.<sup>131</sup> In so doing, the EU law is also touched. The literature has well established the basic features of the reasonableness principle namely suitability, necessity, proportionality, transparency and participation. He suggested that a shift should take place in the sense that the NT principle is employed not only as a prohibition of *de jure* discrimination, but as a tool to review origin-neutral regulation with *de facto* discriminatory or protectionist features. This literature will provide a great reference for this research, but this research will look at it in the view of investment. In Ortino, the comparison is confined to product-related contents, (GATT, Technical Barriers to Trade (TBT) and the EU law relating to goods), but this research will add feature on the comparison with EU freedom of establishment and free movement of capital.

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<sup>129</sup> Juillard, 'Freedom of Establishment, Freedom of Capital Movements, and Freedom of Investment' (n 90).

<sup>130</sup> Aujean, 'The Future of Non-Discrimination – Direct Taxation in Community Law' (n 91).

<sup>131</sup> Ortino, 'From "Non-Discrimination" to "Reasonableness": A Paradigm Shift in International Economic Law?' (n 63).

The discussion on likeness in the international human rights law revolves the human rights context. However, useful observations made by the scholars in the field are helpful in identifying and understanding the practice of the courts in the interpretation and the challenges arising thereof. Among literatures referred to are McColgan,<sup>132</sup> Joory<sup>133</sup> and Gerards.<sup>134</sup>

All of the studies above provide an overview of the existing work relating to this research. This research will fit in and contribute in the scholarship of international investment law with its comprehensive study on the interpretation of likeness and comparative insights from international trade law, the EU and the international human rights law.

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<sup>132</sup> McColgan, ‘Cracking the Comparator Problem: Discrimination, Equal Treatment and the Role of Comparisons’ (n 95).

<sup>133</sup> Joory, ‘Arguments against the Politicized Role of Comparators in Article 14 Discrimination Cases’ (n 95).

<sup>134</sup> Janneke H Gerards, ‘The Discrimination Grounds of Article 14 of the European Convention on Human Rights’ [2013] Human Rights Law Review <<http://hrlr.oxfordjournals.org/content/early/2013/02/13/hrlr.ngs044>>, accessed on 20 February 2013.

## Chapter 2

# THE DOCTRINE OF NATIONAL TREATMENT IN INTERNATIONAL INVESTMENT LAW

### 1.0 Introduction

This chapter will firstly examine the historical origin of national treatment and the development of the doctrine in previous practices. The historical assessment is informative in order to understand the character and importance of the national treatment provision as a fundamental norm in international investment law.<sup>135</sup> It will show how this principle has evolved intensely in recent decades in almost all transnational or international economic agreements as one of the primary protection accorded to foreign investors. In today's context, this principle is fortified by the means of enforcement via investor-state arbitration. This makes it even vital to define its exact scope, application or coverage. This chapter thus identifies the variations of the national treatment provision as in the modern treaty application in the context of investment treaties.

The contextual assessment of the national treatment provision is examined from the investment disputes. It is found that the investment disputes have not adequately reflected or developed the context of the provision to the cases. In responding to this, this chapter importantly analyses these contents by two methods, firstly by looking at

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<sup>135</sup> In a similar vein, Todd Weiler highlights that 'historical analysis is everywhere and always part of international investment law interpretation'. See Todd Weiler, *The Interpretation of International Investment Law: Equality, Discrimination, and Minimum Standards of Treatment in Historical Context* (Martinus Nijhoff Publishers 2013) 1, 17.

the objects and purpose of investment treaties; and secondly by the connection of the national treatment protection to the political economy both at the time of the promulgation of investment treaties and the current time taking into consideration the modern nature of investments. It builds a preliminary overview of the context of national treatment that will be further discussed in depth in Chapter Six with an analysis on the application onto investment disputes.

The next task of this chapter is to evaluate how the tribunals have construed national treatment cases in addressing the question of likeness and legitimate regulatory measures. This chapter will reveal the inconsistencies of the investment decisions in these matters. This thesis generally asserts the importance of coherence with a view that investment tribunal decisions should show some clarity and certainty in the law. This casts implication on the international investment legal order which could otherwise undermine key participants' confidence.<sup>136</sup> Furthermore, with the availability of awards in public, later cases in practice resort to earlier awards.<sup>137</sup> It is therefore essential that awards must be sound in its reasoning.

The discussion of likeness and legitimate regulatory measures in this chapter provides an important foundation for the subsequent comparisons in Chapters Three, Four and Five in the context of GATT/WTO, EU law and International human rights. It also casts an essential basis for the synthesis in Chapter Six for this thesis to

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<sup>136</sup> Thomas W Walde, 'Confidential Awards as Precedent in Arbitrations. Dynamics and Implication of Award Publication' in Yas Banifatemi (ed), *Precedent in International Arbitration* (Juris Publishing Inc. 2008) ; Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

<sup>137</sup> Bjorklund, 'Investment Treaty Arbitral Decisions as Jurisprudence Constante' (n72); Gabrielle Kaufmann-Kohler, 'Arbitral Precedent: Dream, Necessity or Excuse?' (2007) 23 *Arbitration International*, LCIA; Kaufmann-Kohler and International Arbitration Institute, 'Is the Search of Consistency a Myth?' (n 73); Jeffery P. Commission, 'Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence' (2007) 24 *Journal of International Arbitration* 129–158.

present its final suggestion on the criteria and flow of an analysis of likeness in national treatment.

### **National Treatment Obligation – The Origin**

Generally, there was no obligation to treat aliens favourably or in the same position as the locals in customary international law. Such positions were only accorded to in the existence of a particular arrangement or treaty. The Greek for instance, during the time of antiquities or ancient sovereigns have recorded to have given similar treatment to aliens as the locals based on some treaties and the general religious duty of hospitality.<sup>138</sup> The Islamic historical practice has also portrayed a relatively favourable economic environment for foreigners in the form of freedom of commerce.<sup>139</sup>

The modern traces of diplomatic relation among states to protect foreign subjects can however be said to formally begin from the medieval commerce, in particular the formation of the Hansaetic League (1259-1450).<sup>140</sup> The age of colonisation has shown a different landscape in the international economic law. Most of the

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<sup>138</sup> Amos S Hershey, 'History of International Relations During Antiquity and the Middle Ages' (1911) 5 American Journal of International Law 933.

<sup>139</sup> Cameron and Neal, *A Concise Economic History of the World* (n 53); Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3). The interaction between the Italian city states and the Ottoman Empire has adopted the treatment non-less favorable in their diplomatic commercial practice. See Weiler, *The Interpretation of International Investment Law: Equality, Discrimination, and Minimum Standards of Treatment in Historical Context* (n 135) 336.

<sup>140</sup> Georg Schwarzenberger, 'The Province and Standards of International Economic Law' [1948] International Law Quarterly 402. Pieter VerLoren van Themaat, *The Changing Structure of International Economic Laws: A Contribution of Legal History, of Comparative Law and of General Legal Theory to the Debate on a New International Economic Order* (BRILL 1981) 19. Many reference on this matter is referred to Erler's writing, available in German language, see Georg Erler, *Grundprobleme des Internationalen Wirtschaftsrechts. - Göttingen: O. Schwartz 1956.* (Otto Schwartz 1956). See also Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 152.

developing countries were colonised and the foreign investors were mainly the colonists. Thus the treaties were not made with the colonies, possessions or protectorates but mainly between the greater powers.<sup>141</sup> An example of a treaty that contained a national treatment provision from this era was the treaty between Great Britain and Portugal, signed at London on the 29th January 1642. The provision mentioned,

‘And that the subjects of each of the most renowned Kings before named, in the Dominions and Territories of the other, shall not be worse dealt withal than the natural subjects, in their sales and contracts for their merchandizes, as well for price as otherwise; but that the condition of foreigners and natural subjects shall be equal and alike as aforesaid, according to the practice of ancient Treaties made between the most renowned Kings of Great Britain and Castile.’<sup>142</sup>

This treaty also affirms the earlier practice of the national treatment protection between the Kings of Great Britain and Castile. The industrial revolution has later contributed to even more forms of international trade. With the introduction of new technologies and the end of the Napoleonic wars,<sup>143</sup> the world entered into a process

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<sup>141</sup> It was customary that treaties bind the colonies. See Thomas Edward Scrutton and William Bowstead, ‘14 The Commercial Laws of the World Comprising the Bills of Exchange Bankruptcy and Maritime Laws of All Nations’ [1911-1914] *Commercial Treaties and Conventions* 780.

<sup>142</sup> See 2 Hertsllet's *Commercial Treaties: A Complete Collection of the Treaties and Conventions, and Reciprocal Regulations, at Present Subsisting between Great Britain and Foreign Powers* 1(1840) Portugal.

<sup>143</sup> This era introduced new technologies such as the spinning jenny, the use of steel that replaced iron ore, new means of transportation such as the steam engines and communications such as radios. See J Salwyn Schapiro, ‘Industrial Revolution’ (1934) 1 *Modern and Contemporary European History* (1815-1936) 30.



of globalisation.<sup>144</sup> At this stage, more commercial treaties were entered into to encourage international cooperation. Among which were flourishing were the friendship, commerce and navigation treaties (FCN) which were general treaties containing parts of protection of foreign properties.<sup>145</sup> The FCNs were bilateral treaties entered into between states which were generally for the purpose of international cooperation, often containing familiar terms.<sup>146</sup> The Treaty of Friendship, Commerce and Navigation between the United States of America and the Italian Republic for instance provided national treatment in the wordings below,

‘The nationals of either High Contracting Party shall, within the territories of the other High Contracting Party, be permitted, without interference, to exercise, in conformity with the applicable laws and regulations, the following rights and privileges upon terms no less favorable than those now or hereafter accorded to nationals of such other High Contracting Party...’<sup>147</sup>

The US-Japan FCN which was entered into after World War II included a clearer national treatment provision,

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<sup>144</sup> Vandevelde characterised the era between 1820-1914 as the emergence of global economy which marked an active amount of world trade before the advent of World War I. See Vandevelde, *Bilateral Investment Treaties* (n 2) 20.

<sup>145</sup> The first US FCN was entered into in 1778 with France right after its independence.

<sup>146</sup> It must be noted that there are some variation in the main motivation of some treaties, whether more towards friendship or diplomatic ties or commerce, the latter is especially seen in post World War II FCNs. See further discussion in Wayne Sachs, ‘The New U.S. Bilateral Investment Treaties’ (1984) 2 *Berkeley Journal of International Law* 192.

<sup>147</sup> Treaty of Friendship, Commerce and Navigation Between the United States of America and the Italian Republic, signed at Rome, 2 February 1948, Article 1(2). This treaty was applied in the case of *ELSI*. The applicant brought Article 1 of the Supplementary Agreement of the FCN Treaty which prohibited ‘arbitrary and discriminatory’ measures but was dismissed by the Chamber. See *Elettronica Sicula S.p.A. (ELSI) case (United States of America v. Italy)*, Judgment of 20 July 1989.

‘Nationals and companies of either Party shall be accorded national treatment with respect to engaging in all types of commercial, industrial, financial and other business activities within the territories of the other Party, whether directly or by agent or through the medium of any form of lawful juridical entity. Accordingly, such nationals and companies shall be permitted within such territories: (a) to establish and maintain branches, agencies, offices, factories and other establishments appropriate to the conduct of their business; (b) to organize companies under the general company laws of such other Party, and to acquire majority interests in companies of such other Party; and (c) to control and manage enterprises which they have established or acquired. Moreover, enterprises which they control, whether in the form of individual proprietorships, companies or otherwise, shall, in all that relates to the conduct of the activities thereof, be accorded treatment no less favourable than that accorded like enterprises controlled by nationals and companies of such other Party.’<sup>148</sup>

The dimension of such provision in the treaties was to ensure protection of the state party’s citizen in a foreign land for both his person and property. The US-Japan FCN also demonstrates the inclusion of right of establishment, management and control of investment at a level playing field with the locals which are made possible by the national treatment principle.<sup>149</sup> Thus it can be understood that the principle of

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<sup>148</sup> The post world war II FCNs were modified to be more investment related including the national treatment. See Herman Jr Walker, ‘Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice’ (1956) 5 American Journal of Comparative Law 229.; Sachs, ‘The New U.S. Bilateral Investment Treaties’ (n 156).

<sup>149</sup> Treaty and Protocol between the United States of America and Japan (US-Japan Friendship, Commerce and Navigation), signed on 2 April 1953, entered into force on 30 October 1953, <<http://www.mac.doc.gov/japan-korea/market-opening/US-Japan%20Treaty%20on%20Friendship%20Commerce%20and%20Navigation%201953-04-02.pdf>>, accessed on 10 September 2013.

national treatment primarily seeks to provide protection of investment while its furtherance makes liberalisation of trade and investment possible.

It has become somewhat settled during the FCN practice that the investors do not only enjoy level treatment with the locals, they also enjoy a minimum degree of protection under international law if the state protection fall below the line.<sup>150</sup> A heated discussion arose between developed and developing countries over the minimum international standards in which foreign investors are entitled. The developed countries promoted the doctrine of state responsibility for injuries to aliens and their properties that states should adopt the minimum standards of international law which allows foreign investors to be treated better than the treatment accorded to the nationals if the treatment is below the standard. On the other hand, the developing countries, in particular from Latin America defended under the principle of territorial sovereignty that limits the foreign investors to be treated similar to the nationals regardless the international minimum standards.<sup>151</sup> This was later known as the Calvo Doctrine.<sup>152</sup>

In the exchange of correspondence between Cordell Hull, the US Secretary of State and Eduardo Hay, the Mexican Foreign Minister on the expropriation of American landholders in the Mexican agrarian reform, Mexico suggested firmly that the

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<sup>150</sup> Walker, 'Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice' (n 148).

<sup>151</sup> 'International Investment Agreements: Key Issues' (United Nations Conference on Trade and Development 2004) Volume 1 163; 'National Treatment' (United Nations Conference on Trade and Development, UN 1999) 6.

<sup>152</sup> This idea was developed from the idea put forth by Dr. Carlos Calvo in his two volume writings. See Carlos Calvo, *Derecho Internacional Teórico y Práctico de Europa y América* (D'Amyot 1868). See also the discussion in Weiler, *The Interpretation of International Investment Law: Equality, Discrimination, and Minimum Standards of Treatment in Historical Context* (n 135) 417.

standard must be domestic and that foreign investors must not expect better treatment to be given than what is accorded to the locals. In the correspondence:

‘Nationals and foreigners who are under the same protection of the national legislation and authorities the foreigners cannot claim rights different from or more extensive than nationals. The demand for unequal treatment is implicitly included in your Government's note for while it is true that it does not so state clearly, it does require the payment to its nationals, independently of what Mexico may decide to do with regard to her citizens, and as your Government is not unaware that our Government finds itself unable immediately to pay the indemnity to all affected by the agrarian reform, by insisting on payment to American landholders, it demands, in reality, a special privileged treatment which no one is receiving in Mexico.’<sup>153</sup>

The reluctance of adhering to the foreign investors’ demands was a signal from newly independent states that their sovereignty must be respected and acknowledged. It was also to defend the states from forced compensation schemes and arbitration agreements set by capital exporting countries.<sup>154</sup> The impact of non-payment of compensation was very acute during the period due to the capital exporting countries’ possible resort to gunboat diplomacy and military self-help<sup>155</sup> or diplomatic espousal. This would result to economic and political pressure.<sup>156</sup>

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<sup>153</sup> Official Document (1938) 32 AJIL Sup 189.

<sup>154</sup> The injured investor states responded to the inability of weaker countries in paying debts by gunboat diplomacy, which is an abuse of the diplomatic protection process. See Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (Hart 2009).

<sup>155</sup> Luis Maria Drago, an Argentine Foreign Minister stated a firm objection on the use of force for the collection of debt, which later came to be known as the Drago doctrine. See James T Gathii, ‘War’s Legacy in International Investment Law’ (2009) 11 International Community Law Review 353. See

What followed was the number of failures to come up with multilateral investment treaties due to the sensitivity and difficulty of the subject.<sup>157</sup> The unpredictable investment climate, the lack of consensus on customary international law and the inability of states to agree on an accepted international set of protections for investors on a multilateral basis have caused some states to conclude investment treaties on a bilateral basis. Such effort was a more expedite alternative which would provide effective protection to foreign investors and enhance the flow of foreign investment into host states and to benefit from its capital, local employment, skills and technology in the economic development.<sup>158</sup> The facet of today's standard of treatment is no longer chasing for the international minimum standard but more towards wanting the same favourable treatment as given to the local considering the various incentives and advantages provided by the host state.<sup>159</sup>

The first bilateral investment agreement was between Germany-Pakistan in 1959.<sup>160</sup> It was later accumulated up to 2,670 BITs and more than 270 other IIAs at the end of 2008.<sup>161</sup> Among the leading countries with the most investment treaties are

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also José E Alvarez, 'The Emerging Foreign Direct Investment Regime' (2005) 99 Proceedings of the Annual Meeting (American Society of International Law) 94.

<sup>156</sup> Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (n 154) 32.

<sup>157</sup> The multilateral attempts will be explained further in 3.2 'The Political Economy and Nature of Investment' below.

<sup>158</sup> The investment regime was described as an act of hegemonic stability and a cooperative arrangement that would help states to advance their interests. See Salacuse, 'The Emerging Global Regime for Investment' (n 59); Guzman, 'Why LDCs Sign Treaties That Hurt Them' (n 65)

<sup>159</sup> See Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

<sup>160</sup> Germany-Pakistan BIT, signed 25 November 1959, <[http://www.iisd.org/pdf/2006/investment\\_pakistan\\_germany.pdf](http://www.iisd.org/pdf/2006/investment_pakistan_germany.pdf)>, accessed on 4 October 2013.

<sup>161</sup> See 'The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries', UNCTAD Series on International Investment Policies for Development. 2009, <[http://www.unctad.org/en/docs/diaeia20095\\_en.pdf](http://www.unctad.org/en/docs/diaeia20095_en.pdf)>, accessed on 28 January 2014. Most of these agreements contain the national treatment provision.

Germany, China, UK, Switzerland and Egypt.<sup>162</sup> This rapid development was a respond towards both the sponsoring capital exporting countries and the need of the developing countries to build their economies, in most cases, after decolonisation. Capital was needed to build infrastructures and this could be achieved by allowing foreign inflow of capital. In order to create a favourable investment climate, the more familiar Friendship Commerce and Navigation (FCN) templates in the international trade and economic fraternity became handy, and were hence replicated in the new form of investment treaties.<sup>163</sup> These investment treaties include key protective features – expropriation, fair and equitable treatment (FET), full protection and security (FPS), free transfer of fund and most favoured nation (MFN) and national treatment principle.

It is pertinent to mention that some earlier investment treaties did exclude national treatment. A study has shown that of the investment treaties signed before 1990, nearly fifty per cent of them did not include national treatment clauses, especially from the Asian region.<sup>164</sup> The abstention from including national treatment was also due to the reservation of some states so as to the effects of national treatment. Among the western countries which did not insert the national treatment provisions are Sweden and Norway.<sup>165</sup> Following the other investment treaties, the modern Chinese investment treaties have also later begun to include national treatment

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<sup>162</sup> Meredith Broadbent and Robbins Pancake, 'Reinvigorating the U.S. Bilateral Investment Treaty Program' [2012] Center For Strategic & International Studies (CSIS) 4.

<sup>163</sup> The modern BITs have incorporated many features contained in earlier commercial treaties such as the Friendship, Commerce and Navigations (FCN) treaties concluded by the United States. BITs are successors of the FCN programme. See Department of State. (Washington) Warren Christopher. Letter of Submittal. USA-Uzbekistan BIT 1996.<[http://unctad.org/sections/dite/ia/docs/bits/us\\_uzbekistan.pdf](http://unctad.org/sections/dite/ia/docs/bits/us_uzbekistan.pdf)>, accessed on 4 October 2013.

<sup>164</sup> Peter Chowla, 'Comparing Naughty BITs: Assessing the Development Impact of Variation in Bilateral Investment Treaties' [2005] London School of Economics and Political Science <[www2.lse.ac.uk/internationalDevelopment/pdf/WP67.pdf](http://www2.lse.ac.uk/internationalDevelopment/pdf/WP67.pdf)>, accessed on 14 October 2013.

<sup>165</sup> 'International Investment Agreements: Key Issues' (n 151) 87.

provisions. A few examples are the Chinese- Netherlands bilateral investment treaty in Article 3 (3) and the 2008 Free Trade Agreement between Chinese - New-Zealand.<sup>166</sup>

Today, the national treatment obligation is one of the most pivotal obligations in any international investment agreement.<sup>167</sup> It is a treaty based obligation, without which renders host states no obligation to provide foreign investors and nationals similar treatment.<sup>168</sup> Its insertion, accompanied with the dispute resolution clause allows foreign investors to bring direct claims to international arbitration on the ground of discriminatory treatment based on nationality. This position did not exist under customary international law.<sup>169</sup> Although earlier treaties have embodied the national treatment provision, they were applied widely in trade and commerce. Later, the national treatment principle became a common criterion of trade and investment

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<sup>166</sup> China-Netherlands BIT, signed 26 November 2001, entry into force 1 August 2004. < [http://unctad.org/sections/dite/ia/docs/bits/china\\_netherlands.pdf](http://unctad.org/sections/dite/ia/docs/bits/china_netherlands.pdf)>, accessed 23 July 2013; The 2008 Free Trade Agreement between New Zealand and China (NZ-China FTA), signed 7 April 2008, entry into force 1 October 2008, < <http://www.chinafta.govt.nz/1-The-agreement/2-Text-of-the-agreement/index.php>>, accessed 20 July 2013. See also the development of Chinese investment treaties in Norah Gallagher, *Chinese Investment Treaties: Policies and Practice* (Oxford University Press 2009); Axel Berger, 'China's New Bilateral Investment Treaty Programme: Substance, Rational and Implications for International Investment Law Making', *The Politics of International Economic Law: The Next Four Years* (2008), < <http://www.asil.org/files/ielconferencepapers/berger.pdf>>, accessed on 26 July 2013.

<sup>167</sup> See for instance USA-Mongolia BIT, signed 6 October 1994, < [http://unctad.org/sections/dite/ia/docs/bits/us\\_mongolia.pdf](http://unctad.org/sections/dite/ia/docs/bits/us_mongolia.pdf)>, accessed 4 October 2013; Canada-Argentina BIT, signed 5 November 1991, brought into force 29 April 1993, <[http://unctad.org/sections/dite/ia/docs/bits/argen\\_canada.pdf](http://unctad.org/sections/dite/ia/docs/bits/argen_canada.pdf)>, accessed on 20 August 2013, also available at < <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/>>, accessed on 10 September 2013. Australia-Argentina BIT, signed on 23 August 1995, entry into force 11 January 1997, <[http://unctad.org/sections/dite/ia/docs/bits/argentina\\_australia.pdf](http://unctad.org/sections/dite/ia/docs/bits/argentina_australia.pdf)>, accessed on 20 August 2013.

<sup>168</sup> In the absence of contrary rule of international law binding on the States parties, whether of conventional or customary origin, a State may differentiate in its treatment of nationals and aliens. See *Methanex v USA* Part IV - Chapter C - Page 12, para 25. Similarly, in the case of *Genin v Estonia*, the tribunal confirmed that 'Customary international law does not, however, require that a state treat all aliens (and alien property) equally, or that it treats aliens as favourably as nationals.' See *Genin, Eastern Credit Ltd. Inc. and AS Baltoil v Republic of Estonia*, Award, 25 June 2001, para 368.

<sup>169</sup> Gus Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford University Press 2007) 9. Under customary international law, a claim can only be made by diplomatic protection which discretion rests upon the home state.

treaties in modern international economic law.<sup>170</sup> In the investment context, the national treatment principle is developed by its adoption in international investment treaties and its interpretation in investment arbitration awards.

## **2.0 National Treatment Provisions: Scope and Treaty Practices**

The ordinary phrasing of the national treatment provision across BITs generally comprises of an obligation that the contracting parties must accord treatment ‘no less favourable’ to the investors or investments of the other contracting party than that they accord to their nationals ‘in like circumstances’. Article 3 of the US-Rwanda BIT 2008 provides national treatment in the following wordings;

‘1. Each Party shall accord to investors of the other Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.

2. Each Party shall accord to covered investments treatment no less favorable than that it accords, in like circumstances, to investments in its territory of its own investors with respect to the establishment, acquisition, expansion,

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<sup>170</sup> Thomas W Walde, ‘In the Arbitration Under Article 26 Energy Charter Treaty (ECT), *Nykomb V. The Republic of Latvia-Legal Opinion*’ (2005) 2 *Transnational Dispute Management (TDM)*., para 102. See also Todd Weiler, ‘Prohibitions Against Discrimination in NAFTA Chapter 11’ in Todd Weiler (ed), *NAFTA Investment Law and Arbitration: Past Issues, Current Practice, Future Prospects* (Transnational Publishers 2004) 28.



management, conduct, operation, and sale or other disposition of investments.’<sup>171</sup>

The inclusion of less favourable treatment is an advantageous standard of treatment from the investors’ viewpoint. This reflects the debate in the past as to what level the treatment should be given. In the past, the national treatment principle was used to limit foreign investors from enjoying more treatment than the locals by the invocation of international minimum standard of treatment. Today, in the era where states are giving incentives to the locals, the national treatment provision is used by the foreign investors to obtain these advantages.<sup>172</sup>

National treatment covers both *de jure* and *de facto* discrimination.<sup>173</sup> In determining less favourable treatment, the tribunal would look at the factual impact of the discriminatory measure. There is no requirement of weighing the proportionate or disproportionate advantages as to its quantifications, but it may be indicative as a matter of ‘identification’ of a particular nationality being discriminated.<sup>174</sup> In the context of investment treaties, what matters is under the investor’s exercise of its

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<sup>171</sup> US-Rwanda BIT, signed 19 February 2008, <[http://unctad.org/sections/dite/ia/docs/bits/US\\_Rwanda.pdf](http://unctad.org/sections/dite/ia/docs/bits/US_Rwanda.pdf)>, accessed on 4 October 2013.

<sup>172</sup> Walde regarded today’s conception of national treatment as a ‘minimum standard’ as opposed to the Calvo’s ‘maximum’ or ‘absolute ceiling’. He also referred to it as treatment being ‘pulled up’ in the former and ‘pulling down’ in the latter. See Walde, ‘Comments on the Discipline of ‘National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3).

<sup>173</sup> *ADF Group Inc v United States of America* ICSID Case No ARB (AF)/00/1, 9 January 2003, 18 ICSID Rev-FILJ 195 (2003), para 157; *El Paso Energy International Co v Argentine Republic* ICSID Case No ARB/03/14, Decision on Jurisdiction, 27 April 2006, para 309. See also ‘Non-Discriminatory Barriers to Establishment’ (Organisation for Economic Co-operation and Development 1996) Negotiating Group on the Multilateral Agreement on Investment (MAI) DAF/MAI(96)28 <<http://www.oecd.org/daf/mai/pdf/ng/ng9628e.pdf>>. <<http://www.oecd.org/daf/mai/pdf/ng/ng9628e.pdf>>, accessed on 26 July 2013.

<sup>174</sup> *Pope & Talbot, Inc. v Canada*, (n 20), para 55.

own right, whether there was less favourable treatment as compared to other investors in like circumstances.<sup>175</sup>

Some provisions are combined with the most favoured nation principle as in the US-Czech Republic 1992 BIT,

‘Each Party shall permit and treat investment, and activities associated therewith, on a basis no less favorable than that accorded in like situations to investment or associated activities of its own nationals or companies, or of nationals or companies of any third country, whichever is the most favorable, subject to the right of each Party to make or maintain exceptions falling within one of the sectors or matters listed in the Annex to this Treaty.’<sup>176</sup>

There are investment treaties which do not contain the comparison between like circumstanced or situated investments. The UNCTAD inferred this absence to a much wider scope of comparison.<sup>177</sup> This was raised in the MAI negotiations over the national treatment provision. Some delegates asserted that its inclusion is unnecessary and should be implicitly required.<sup>178</sup>

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<sup>175</sup> The right of national treatment is dependent on the claimant’s own facts and own deprivation of investment. See Canada’s argument on disproportionate disadvantage and the tribunal’s response in *Pope & Talbot, Inc. v Canada*, (n 20), para 44-56.

<sup>176</sup> US-Czech Republic BIT, signed October 22, 1991, entered into force 19 December 1992, <[http://unctad.org/sections/dite/ia/docs/bits/czech\\_us.pdf](http://unctad.org/sections/dite/ia/docs/bits/czech_us.pdf)>, accessed 20 July 2013.

<sup>177</sup> ‘National Treatment’ (n 151) 34.

<sup>178</sup> ‘National Treatment, Non-Discrimination/MFN and Transparency’ (Organisation for Economic Co-operation and Development 1996) Negotiating Group on the Multilateral Agreement on Investment (MAI) D AFPE/MAI/DG2(95)1/REV2 <<http://www.oecd.org/daf/mai/pdf/dg2/dg2951r2e.pdf>>. <<http://www.oecd.org/daf/mai/pdf/dg2/dg2951r2e.pdf>>, accessed on 26 July 2013.

The national treatment provisions in international investment law generally contain a high degree of homogeneity even though the BITs were separately concluded. All national treatment provisions prohibit different treatments of foreign investments/ investors as compared to those given to the locals. Some noticeable differences however are the usage of the term ‘situations’ rather than ‘circumstances’,<sup>179</sup> ‘similar’ rather than ‘like’ or ‘same’, ‘as favourable as’ or ‘no less favourable’ treatment or whether they are inserted as stand-alone or combined with other general standards of treatment.<sup>180</sup>

The national treatment provision are sometimes not termed in the familiar language as in the US-Rwanda BIT and US-Czech Republic BIT above which contain less favourable treatment and like circumstances or like situations. They sometimes appear in a more general prohibition of arbitrary and discriminatory measures. The FCNs generally contain these clauses. The interpretation of such clauses have been similar to an assessment of a claim under national treatment as it involves the same questions, i.e whether there was less favourable treatment, proper comparator and reasonableness of the measure.<sup>181</sup> An example of a bilateral investment treaty which contains a prohibition of this kind is the U.S-Ecuador BIT 1993.<sup>182</sup>

The national treatment provision contained in Article 1102 in NAFTA is the most invoked provision in investment cases, among others were *Pope & Talbot Inc v Canada*, *SD Myers Inc. v Canada*, *CPI v Mexico*, *Cargill, Inc v Mexico* and

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<sup>179</sup> See, e.g Article 1102, NAFTA. In some other BITs, predominantly US BITs, the term used is ‘in like situations’. See e.g, US-Bolivia BIT 1998, <<http://www.state.gov/documents/organization/43541.pdf>>, accessed on 4 October 2013

<sup>180</sup> ‘National Treatment’ (n 151).

<sup>181</sup> See *Elettronica Sicula S.p.A (ELSI) (United States of America v. Italy)*, (n147).

<sup>182</sup> Art II (3)(b), invoked in *OEPC v Ecuador*, (n 18), para 157.

*Methanex v USA*. Examples of other cases outside NAFTA were *OEPC v Ecuador* under the US-Ecuador BIT, *Champion Trading Co. v Egypt* under the US-Egypt BIT and *Noble Ventures v Romania* under ECT.<sup>183</sup>

The scope of the national treatment provision depends on the extent given in the treaties. Some treaties provide coverage for pre-establishment while others limit it to established investments. Most investment treaties provide the protection to established investments only. The Energy Charter Treaty for instance in Article 10 (7) provides:

‘Each Contracting Party shall accord to Investments in its Area of Investors of other Contracting Parties, and their related activities including management, maintenance, use, enjoyment or disposal, treatment no less favourable than that which it accords to Investments of its own Investors or of the Investors of any other Contracting Party or any third state and their related activities including management, maintenance, use, enjoyment or disposal, whichever is the most favourable.’<sup>184</sup>

On the other hand, the 2004 Canadian Foreign Investment Protection Agreements (known as the Canadian FIPAs) in its article 4 stipulates a broad coverage of investment activities including pre-establishment;

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<sup>183</sup> See *Pope & Talbot Inc v Canada* (n 20); *S.D. Myers Inc. v Canada*, (n24), *CPI, Inc v Mexico*, (n 98), *Cargill, Incorporated v. United Mexican States* ICSID Case No. ARB(AF)/05/2, Award, 18 September 2009; *Methanex USA*, (n19); *OEPC v Ecuador*, (n18); *Champion Trading Company and Others v Arab Republic of Egypt*, ICSID Case No. ARB/02/9, 27 October 2006 and *Noble Ventures Inc. v. Romania* ICSID Case No. ARB/01/11, October 12, 2005.

<sup>184</sup> The Energy Charter in Part III provides for investment promotion and protection. See The Energy Charter Treaty and Related Documents. <[http://www.encharter.org/fileadmin/user\\_upload/document/EN.pdf](http://www.encharter.org/fileadmin/user_upload/document/EN.pdf)>, accessed on 16 July 2013.

- ‘1. Each Party shall accord to investors of the other Party treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments in its territory.
2. Each Party shall accord to covered investments treatment no less favourable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments in its territory.’

This resembles the NAFTA and the 2004 US Model treaties that include pre-establishment protection of foreign investors.<sup>185</sup> Similarly, pre-establishment clause is included in Article 10.3, Chapter 10 of CAFTA.<sup>186</sup> The recent Japanese BITs are also of this feature.<sup>187</sup> In the selection of words to describe investment activities in a national treatment provision, the OECD Commentary Draft of the MAI has made a helpful remark. The Group agreed that all diversification activities are covered by the references to “establishment, acquisition and expansion”. The commentary further stated:

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<sup>185</sup> See for instance US-Uruguay BIT 2005, Article 3 under the 2004 US Model treaties template, signed November 2005, < [http://unctad.org/sections/dite/ia/docs/bits/US\\_Uruguay.pdf](http://unctad.org/sections/dite/ia/docs/bits/US_Uruguay.pdf)>, accessed on 4 October 2013.

<sup>186</sup> Central America Free Trade Agreement (CAFTA) comprises of the Government of the Republic of Costa Rica, the Government of the Dominican Republic, the Government of the Republic of El Salvador, the Government of the Republic of Guatemala, the Government of the Republic of Honduras, the Government of the Republic of Nicaragua, and the Government of the United States of America < <http://www.caftalaw.net/cafta-text>>, accessed on 20 July 2013.

<sup>187</sup> See for instance Korea-Japan BIT 2002, signed 22 March 2002, entry into force 1 January 2003, < [http://unctad.org/sections/dite/ia/docs/bits/korea\\_japan.pdf](http://unctad.org/sections/dite/ia/docs/bits/korea_japan.pdf)>, accessed on 20 August 2013, and Japan-Lao Peoples’ Democratic Republic BIT 2008, signed 16 January 2008, < [http://unctad.org/sections/dite/ia/docs/bits/Japan\\_Laos.pdf](http://unctad.org/sections/dite/ia/docs/bits/Japan_Laos.pdf)>, accessed on 20 August 2013. Peter Chowla, ‘Comparing Naughty BITs: Assessing the Development Impact of Variation in Bilateral Investment Treaties’ (n 164) 18.

‘Several Delegations believed that the list “establishment, acquisition, expansion, operation, management, maintenance, use, enjoyment and sale or other disposition of investments” should be considered a comprehensive one whose terms were intended to cover all activities of investors and their investments for both the pre- and post-establishment phases. In their view, this was the preferable approach.’<sup>188</sup>

There are treaties that have national treatment negative list of exceptions. These lists are normally representing strategic industries that the states want to be excluded from the liberalisation process.<sup>189</sup> In the USA-Mongolia BIT for instance, the US government specified a list of sectors and matters which are excluded from national treatment inter alia air transportation, ocean and coastal shipping, banking, energy and power production and communication services. Mongolia’s exceptions were land ownership and banking.<sup>190</sup> The US exceptions in the US-Bolivia BIT from national treatment obligation are:

‘Atomic energy; customhouse brokers; licenses for broadcast, common carrier, or aeronautical radio stations; COMSAT; subsidies or grants, including government-supported loans, guarantees, and insurance; State and local measures exempt from Article 1102 of the North American Free Trade

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<sup>188</sup> OECD, ‘The Multilateral Agreement on Investment Commentary to the Consolidated Text’ (Organisation for Economic Co-operation and Development 22 April 1998) Negotiating Group on the Multilateral Agreement on Investment (MAI) 9, <<http://www1.oecd.org/daf/mai/pdf/ng/ng988r1e.pdf>>, accessed on 4 October 2013.

<sup>189</sup> Such as infant industries that may not be able to compete with foreign investors, natural resources or essential public utilities. See ‘International Investment Agreements: Key Issues’ (n 151) 109 <[http://unctad.org/en/Docs/iteit200410\\_en.pdf](http://unctad.org/en/Docs/iteit200410_en.pdf)>, accessed on 16 July 2013.

<sup>190</sup> US-Mongolia BIT, signed 6 October 1994, <[http://unctad.org/sections/dite/ia/docs/bits/us\\_mongolia.pdf](http://unctad.org/sections/dite/ia/docs/bits/us_mongolia.pdf)>, accessed on 4 October 2013.

Agreement pursuant to Article 1108 thereof; and landing of submarine cables.’<sup>191</sup>

The OECD has organised a programme for South Eastern Europe (SEE) countries which analyses the exceptions in the field of authorization, licensing and screening procedures in various sectors of the SEE.<sup>192</sup> The prevalent exceptions are in foreign real estate ownership, while sector wise are in the areas of insurance, maritime transport and fishing. The OECD also provides updates of exceptions from national treatment by OECD countries and eight non-member economies. The recent 2013 report listed the exceptions as a measure to provide transparency among the states.<sup>193</sup>

In connection to this, it is hard to say that investment treaties are going towards full liberalisation. As compared to MAI, the BITs are focused on the protection of investments. The MAI involved OECD countries which were ready to embark on ‘a broad multilateral framework for international investment with high standards for the liberalisation of investment regimes and investment protection and with effective dispute settlement procedures’. As explained earlier, the scope in the application of national treatment differs. Even in treaties that grant pre-establishment, they have negative list of exceptions. The treaties such as the Canadian FIPA, NAFTA and US treaties allow exception annex to national treatment. The Canadian FIPA for instance in Article 9 has excluded government of state enterprise procurement, subsidies or

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<sup>191</sup> US-Bolivia BIT 1998, (n179).

<sup>192</sup> National Treatment of International Investment in South East European Countries- OECD 2003, p13, < <http://www.oecd.org/investment/investmentfordevelopment/20637291.pdf>>, accessed 15 October 2013.

<sup>193</sup> National Treatment for Foreign Controlled Enterprises: Including Adhering Countries Exceptions to National Treatment. 2013 < <http://www.oecd.org/daf/inv/investment-policy/national-treatment-instrument-english.pdf>>, accessed on 28 January 2014.

grants including government supported loans, guarantees and insurance. A similar trait can be found in the US 2004 Model BIT in Article 14.

These are the exact reasons why some investment treaties are called as adopting ‘selective liberalisation’.<sup>194</sup> It is submitted that liberalisation in the contexts of international investment agreement differ to that of GATT/WTO, as it provides liberalisation within the area permitted. It has a limited connotation depending on the scope of the treaties and should not be overemphasised in the interpretation of national treatment.

The issue of BITs as promoting ‘protection’ or ‘liberalisation’ is related to the treaty designs of recent investment treaties (especially the FTAs incorporating investment chapters). Marino Baldi described that investment protection rules have clear characteristics of property law while investment liberalisation rules have a trade-policy character.<sup>195</sup> This constitutes a theoretical difficulty that will be faced by these new generations of investment treaties which would probably cast a more challenging balancing of sovereign and foreign investors’ interest.

### **3.0 The Contextual Analysis**

The minimalist approach in the drafting of the national treatment provisions has left the tribunals a huge task to determine its interpretation. The tribunals have to fulfil the legal requirements of ‘less favourable treatment’ and ‘in like circumstances or

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<sup>194</sup> ‘Admission and Establishment’ (United Nations Conference on Trade and Development, UN 2002) 39.

<sup>195</sup> Baldi, ‘Less May be More: the Need for Moderation in International Investment Law’ (n 51) 448.



situations’, in the right contextual framework. The context should be instructive on the tribunals as to the purpose of national treatment in the context of international investment law. This would in turn guide the balance between the investors’ protection and the host states’ regulatory space. It is observed that the contextual aspect of the national treatment interpretation is an underdeveloped area in investment tribunal decisions.

This is a challenging matter as there is limited, if any, legal textual documentations or the preparatory work (*travaux*) that could explain the context of national treatment in investment treaties.<sup>196</sup> This adds the pressure that has already surrounded investment tribunals that investment law is different to trade, causing the tribunals to exercise caution to refer to the latter. While the differences in wordings do not linguistically and substantially differentiate the essence of the protection from one BIT to another, the interpretation of the terms in the context of national treatment however proves to be interestingly challenging and diverged. In any exercise of comparison, the comparator must be of a common denominator. Past arbitrations have suggested at times that the common denominators should be ‘common competitive investments’ or of ‘common economic sector’.<sup>197</sup> At some other instances, the comparators are considered common if they share ‘common economic activity’ regardless of the economic sector.<sup>198</sup> In many cases, the appropriate

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<sup>196</sup> The preparatory works of investment treaties are often unavailable. A notable exception is NAFTA. See NAFTA negotiating texts available at < <http://www.naftalaw.org/commission.htm>>, accessed on 17 October 2013. See also Meg Kinneer, Andrea Bjorklund and John FG Hannaford, *Investment Disputes Under NAFTA: An Annotated Guide To NAFTA Chapter 11* (Kluwer Law International 2006). In cases where they are available, they are rarely used for the interpretation of substantive provisions. Fauchald, ‘The Legal Reasoning of ICSID Tribunals – An Empirical Analysis’ (n69); ‘The Usefulness of Travaux in Investment Treaty Interpretation’ (2005) 2 Transnational Dispute Management (TDM) <<http://www.transnational-dispute-management.com/article.asp?key=442>> accessed 28 July 2013.

<sup>197</sup> *Pope & Talbot Inc. v. Canada*, (n 20), para 78.

<sup>198</sup> *OEPC v Ecuador*, (n 18), para 168.

comparator test is regarded by whether they were ‘common from the viewpoint of the regulatory measure challenged’, which is a very broad approach.

The approaches provided by past arbitrations are nevertheless valuable in identifying some areas of comparison, but the decisions collectively lacked the contextual flavour and doctrinal clarity, which may not necessarily bring to a different conclusion in the award, but to a sound judgment which greatly contributes to the coherence of the jurisprudence. The most important foundation for a sound regime is therefore the establishment of a clear contextual layout of its doctrines. The quest for a contextual understanding of national treatment must begin with the objects and purpose of its introduction, the scope of national treatment, the investment climate which it is expected to serve and the crux of its discriminatory characteristic which distinguishes it from other discriminations.

There are at least two methodologies that could indicate the understanding of the context of national treatment in investment treaties. Firstly, by looking at the objectives and purposes of the treaties as commonly found in the preambles and secondly the political economy of both times- the time of the promulgations of investment treaties and the historical evolution of previous attempts of a network of investment protection regime; and the current political economy of world investment.<sup>199</sup>

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<sup>199</sup> A third methodology, that is by comparing the context of the non-discrimination principle based on nationality in the GATT/WTO, EU and IHR jurisprudence will be introduced and elaborated in Ch. 6 of this thesis. This would be in consistent with Articles 31-32 of the VCLT which requires the search of the context of the provision. See *Methanex v USA*, Final Award Part IV Chapter B para 29, p14. See also *International Thunderbird Gaming Corporation v. United Mexican States* (hereinafter, ‘*Thunderbird Case*’) UNCITRAL, Award, 26 January 2006, para 175. ‘The interpretation of treatment standards in investment treaties must begin, like any other process of treaty interpretation with the approach indicated by Articles 31 and 32 of the Vienna Convention on the Law of Treaties

### 3.1 The Objects and Purpose of National Treatment

In every attempt to interpret national treatment, one must not lose sight of the object and context of its existence in international investment law.<sup>200</sup> It is the first step towards a contextual interpretation of national treatment, but this link needs to be articulated.<sup>201</sup> A notable attempt however that searched the overall context is the case of *Pope & Talbot v Canada* in defining like circumstances. The tribunal agreed that the legal context of Article 1102 as proposed by the claimant includes the trade and investment-liberalising objectives of the NAFTA.<sup>202</sup> By comparing investments in the same business or economic sector, the tribunal believed that it would reflect the legal context of Article 1102.<sup>203</sup>

In the case of *SD Myers Inc. v Canada*, the tribunal examined the preambles of NAFTA, NAAEC and other international commitments to look at a wider context of which NAFTA Chapter 11 and national treatment comes in place. The tribunal also took into account the various provisions of NAFTA and NAAEC which includes states' rights to establish high levels of environmental protection, avoidance of distortions in trade and mutually supportive environmental protection and economic development. As the case was involving environmental regulatory measure, the tribunal tried to determine both environmental concern and the need to avoid trade distortions that are not justified by environment concerns.<sup>204</sup>

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1969'. See Campbell McLaghlan, Laurence Shore and Mathew Weiniger, *International Investment Arbitration: Substantive Principles* (New York: OUP, 2007) 221.

<sup>200</sup> Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3) 24.

<sup>201</sup> Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 152.

<sup>202</sup> *Pope & Talbot Inc. v. Canada*, (n 20), para 77.

<sup>203</sup> *Ibid*, para 78.

<sup>204</sup> *S.D. Myers, Inc. v Canada*, (n 24), para 62.

The approach taken in *SD Myers Inc. v Canada* was however more towards searching the relevance of environmental protection with the national treatment obligation in NAFTA. While such approach is essential in determining the scope of the NAFTA national treatment provision,<sup>205</sup> it was not comprehensive. The tribunal should have deliberated further on the objective of national treatment in the context of promoting and protecting the security of investments as the first step, and then its interplay with the state's commitment in the environmental treaties in question.

The attempt to appreciate the objectives and purpose of national treatment such as in *Pope & Talbot v Canada* and *SD Myers Inc. v Canada* in the search of its contextual interpretation is not often found in arbitral decisions. Tribunals tend to pave away with single issues while interpreting national treatment, with which they conclude. In the separate statement of *UPS v Canada*,<sup>206</sup> the tribunal focused on the differences of the investors in detail rather than deliberating on the apparent competitive relationship and the importance of investment protection which could have led to a contextual interpretation of national treatment.

The preambles of investment treaties are normally broadly drafted. Most of the bilateral investment treaties are entitled 'promotion and protection of investments'. The Germany-Bangladesh BIT for instance further provides the aim to 'create favourable conditions for investments by nationals and companies of either states' and that the promotion and reciprocal protection of such investments 'are apt to

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<sup>205</sup> As international investment emerge in the middle of other branches of international law, awareness of such wider international concerns is essential in determining the scope and application of national treatment.

<sup>206</sup> See *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, 24 May 2007, paras 14-17.

stimulate private business initiative and to increase the prosperity of both nations’.<sup>207</sup>

The NAFTA in Article 102 states in relation to investments that it aims to ‘increase substantially investment opportunities in the territories of the Parties’. The Energy Charter Treaty states ‘to catalyse economic growth by means of measures to liberalize investment and trade in energy’.<sup>208</sup> These preambles can generally conclude that investment treaties are aimed to facilitate the maintenance and protection of investments and the promotion thereof against possible domestic legal uncertainties. It aims at providing a level playing field and favourable investment climates by way of the substantive provisions, in particular on expropriation, national treatment, fair and equitable treatment and full protection and security. These protections are further guaranteed by the investor-state dispute resolution mechanism which enables the foreign investor a direct recourse in an independent tribunal.

Earlier attempts to create multilateral investment treaties also did not provide a clear guidance in the essence of national treatment. The Abs-Shawcross draft was among the earliest to address a multilateral approach of foreign investors protection.<sup>209</sup> The Abs-Shawcross draft provided a general protection of foreign investments against unreasonable or discriminatory measures.<sup>210</sup> Similarly, the Harvard draft and the

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<sup>207</sup> Germany-Bangladesh BIT, 6 May 1981, <[http://unctad.org/sections/dite/ia/docs/bits/germany\\_bangladesh.pdf](http://unctad.org/sections/dite/ia/docs/bits/germany_bangladesh.pdf)>, accessed on 29 July 2013. Similarly, favourable conditions is also found in the Denmark-Malaysia BIT (1992), <[http://unctad.org/sections/dite/ia/docs/bits/denmark\\_malaysia.pdf](http://unctad.org/sections/dite/ia/docs/bits/denmark_malaysia.pdf)>, accessed on 20 August 2013.

<sup>208</sup> Preamble, The Energy Charter Treaty, Annex 1, Official Journal of the European Communities, L69/26, March 1998, <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:1998:069:0026:0090:EN:PDF>>, accessed on 29 July 2013.

<sup>209</sup> Seidl-Hohenveldern, ‘Abs-Shawcross Draft Convention to Protect Private Foreign Investment’ (n 55). See also Michael Brandon, ‘Recent Measures to Improve the International Investment Climate’ (1960) 9 Journal of Public Law 125.

<sup>210</sup> 1959 Draft Convention on Investments Abroad (Abs-Shawcross Draft Convention), (n 55).

OECD draft which came later provide similar protection but did not have expressed reference to the national treatment clause.<sup>211</sup>

The OECD 1976 *Declaration on International Investment and Multinational Enterprises* (the OECD Declaration) for instance provides a guideline accompanying its national treatment provision.<sup>212</sup> Enterprises within the OECD states must maintain the environment, public health, safety and labour rights. NAFTA also recognises that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures.<sup>213</sup> The defined area of application in some investment treaties has shed light to investment arbitrations in delivering decisions. They also indirectly form the exceptions similar to, although not as extensive as the general exceptions in Article XX in the GATT jurisprudence.

One would realise that the national treatment protection has an immense role in achieving the objects and purpose of investment treaties. It battles innate domestic regulations that discriminate foreign investors even on a *de facto* basis. It is a form of an external discipline that alerts discriminatory effects of nationally neutral measure imposed by host states under various reasons such as the environment or public health.<sup>214</sup> Many of the cases brought under national treatment are of this nature, for instance the export ban on polychlorinated biphenyl (PCBs) in *SD Myers Inc v Canada* and the ban on MTBE in the case of *Methanex v USA*. These are delicate

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<sup>211</sup> 1961 Draft Convention on the International Responsibility of States for Injuries to Alien (1961 Harvard Draft); 1967 OECD Draft Convention on the Protection of Foreign Property, )1968) 7 ILM 117 (OECD Draft), (n 57).

<sup>212</sup> Article II.1, OECD 1976 Declaration on International Investment and Multinational Enterprises, (n 58).

<sup>213</sup> NAFTA, Article 1114.

<sup>214</sup> Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

matters that tribunals have to construe in demarcating legitimate and reasonable measures against discriminatory effects on foreign investors. The national treatment principle should ideally be able to prohibit such *de facto* discriminations (apart from *de jure*) as per committed by the signing parties of investment treaties acknowledging national treatment as a treaty based obligation. Without the incorporation of the national treatment provision, the states are certainly disbarred from discriminating foreign investors in favour of the locals.<sup>215</sup> It must be seen as to discipline governments in regulating in a manner that suits the rule of law which is a necessary ingredient for a workable global economy.

The essence of international investment agreement containing the national treatment principle must constantly be emphasised in arbitral decisions. The national treatment principle in today's treaties is a product of mutual understanding by the contracting parties. States entering BITs agree that they will not treat the investors of the other party less favourably than what it accords to its own investors. This commitment is so vital that states are ready to relinquish certain sovereign privilege that would have enabled them to introduce regulatory measures which grant protectionism to its investors in the local industry.<sup>216</sup>

This compromise is a result of recognising the bigger benefit of foreign direct investment, including job opportunities, transfer of skills and technology and development of infrastructures. States also benefit from the flow of capital by its

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<sup>215</sup> It is stated in *Methanex v USA* that 'In the absence of a contrary rule of international law binding on the State parties, whether of conventional or customary origin, a State may differentiate in its treatment of nationals and aliens. See *Methanex v USA*, (n 19), Part IV- Chapter C, paras 14-15. See also national treatment as a treaty-based obligation in Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 149.

<sup>216</sup> Despite this disadvantage, states still enter into investment agreements. See Guzman, 'Why LDCs Sign Treaties That Hurt Them' (n 65).

investors. The bigger benefit of foreign direct investment is believed to be achieved if foreign investment is promoted and protected. Thus most of the BITs emphasise the aim to promote, variedly in terms such as ‘promotion of investment relations’,<sup>217</sup> ‘promotion and protection of investments of investors’<sup>218</sup> and ‘to create favourable conditions for investments’.<sup>219</sup> The preamble of NAFTA also explicitly asserts that the Parties will ensure a predictable commercial framework for business planning and investment which is essential to protect investments from unpredictable changes in the domestic regulations.

The national treatment provision is the cornerstone in almost all investment treaties because of its potential to promote investment protection and security, especially of its functional survival in an alien land. An investment which is deprived functionally by way of discriminatory regulatory measure may be fatal to its survival or existence. Among the consequences includes loss of sales and profits, loss of investments or joint venture,<sup>220</sup> destruction or cutting access of market<sup>221</sup> and massive increase of operational cost.<sup>222</sup>

An observation of the objects and purpose of the national treatment provision must include nationality as its main essence of protection. It differentiates from ordinary discrimination where nationality is not a factor. The claimant needs to show that

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<sup>217</sup> See, e.g. Australia-Argentina BIT 1995 (n 167).

<sup>218</sup> See, e.g. Canada-Argentina BIT 1991, <[http://unctad.org/sections/dite/ia/docs/bits/argen\\_canada.pdf](http://unctad.org/sections/dite/ia/docs/bits/argen_canada.pdf)>, accessed on 20 August 2013.

<sup>219</sup> See, e.g. China-Belgium BIT 1984, [http://unctad.org/sections/dite/ia/docs/bits/china\\_belg\\_lux.pdf](http://unctad.org/sections/dite/ia/docs/bits/china_belg_lux.pdf), accessed on 20 August 2013.

<sup>220</sup> SDMI claimed that among the result of Canada’s breach of obligation under NAFTA is the loss of its investment in its joint venture with Myers Canada. See *SD Myers Inc. v Canada*, (n 24), para 144.

<sup>221</sup> The CPI claimed that the Mexican government destroyed the soft drinks market for HFCS to the benefit of the Mexican sugar industry. *CPI Inc. v Mexico*, (n 98), para 83.

<sup>222</sup> The impact of not allowing fabricating steel in Canada has caused increase of cost due to the hiring of five U.S fabricators, testing, equipment rental, transport, demurrage and additional time in project management. See *ADF Group Inc v USA* (n 173), para 55.



there is direct or indirect actual discrimination which affect foreign investors only. In the determination of in like circumstances, the nationality test is crucial. The foreign investor or foreign owned investment should be compared to a domestic owned investment that is like in all relevant respects, but for nationality of ownership.<sup>223</sup> In *Feldman v Mexico*, the tribunal mentioned:

“In this instance, the evidence on record demonstrates that there is only one U.S Citizen/ investor, the Claimant, that alleges a violation of national treatment under NAFTA Article 1102, and at least one domestic investor who has been treated favourably. For practical as well as legal reasons, the Tribunal is prepared to assume that the differential treatment is a result of the Claimant’s nationality, at least in the absence of any evidence to the contrary”.<sup>224</sup>

Tribunals must determine whether the measures explicitly discriminate or adversely impact foreign investors.<sup>225</sup> Discriminatory motive does not necessarily emerge in the measure but can be examined from the impact of the measure. It thus involves *de jure* and *de facto* examination in national treatment cases. In the case of *SD Myers Inc. v Canada*, the ban of disposing PCBs originating from Canada to United States by *de facto* nationally discriminated Canadian investors. In the case of *Feldman v Mexico* the tribunal concluded that Mexico has violated national treatment provision on the basis of nationality by denying tax rebates for cigarettes sold for export to a US company.<sup>226</sup> The decision of *OEPC v Ecuador* case on the other hand was not

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<sup>223</sup> *Methanex v USA*, (n 19), para14.

<sup>224</sup> *Feldman v Mexico*, (n 15), para 181.

<sup>225</sup> Vandevelde, *Bilateral Investment Treaties* (n 2) 377.

<sup>226</sup> *Feldman v Mexico*, (n 15), para 182.

examined based on nationality but the different treatment across sectors as no exporter can be discriminated against other exporters.<sup>227</sup>

### 3.2 *The Political Economy & Nature of Investments*

One would have to trace the underlying philosophy of the investment treaties in the history of its evolution. The crucial turning point in the history of investment regime was the global collapse of the economy between 1914-1944.<sup>228</sup> The international investment regime suffered during this period as foreign properties were seized and nationalised.<sup>229</sup> According to Verloren Van Themaat, the period between the two world wars is significant to the evolution of international economic law because it was in this period that many of the principles of treaty law that have evolved during the preceding seven centuries has disappeared.<sup>230</sup> Post war U.S FCNs responded to the calamity of the war on foreign investments by including detailed rules on expropriation and the principle of non-discrimination.<sup>231</sup> It is important to understand what led to the promulgation of the national treatment provision during this time.

Direct mention on the matter is scarce. However, indication can be made from observations and pieces of information from separate events and evolution. At this particular point, the idea of economic liberalism emerged and dominated the earlier

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<sup>227</sup> *OEPC v Ecuador*, (n 18), para 176. See also Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 152.

<sup>228</sup> Schwarzenberger, 'The Province and Standards of International Economic Law' (n 140).

<sup>229</sup> Vandeveldel highlighted how the principles of non-discrimination, the principle of access and security which were once enjoyed before the World War 1 were ignored. Countries seized enemy properties. As far as nationalization is concerned, the series of expropriations of foreign investment by the Soviet government in the 1920s was a striking example. See Vandeveldel, *Bilateral Investment Treaties* (n 2) 31–35.

<sup>230</sup> Themaat, *The Changing Structure of International Economic Laws* (n 140) 21.

<sup>231</sup> For instance, US-Netherlands FCN, signed 27 March 1956, entered into force 5 December 1957, <<http://www.minbuza.nl/en/key-topics/treaties/search-the-treaty-database/1956/3/008392.html>>, accessed on 3 October 2013 and US-Japan FCN (n 149).

theory of mercantilism which discouraged exports.<sup>232</sup> Under this theory, state intervention would be a barrier of economic efficiency. Liberalism was supported by the classical economists including David Ricardo and John Stuart Mill who were inspired by earlier works of Adam Smith.<sup>233</sup> This evolution was coupled with the prevalence of the *laissez faire* principle which maintained liberty to trades and individuals in the economic activity from the interference of the state.<sup>234</sup>

Vandevelde tried to match the development of investment treaties with the relevant economic theory.<sup>235</sup> The investment treaties are clearly inclined towards liberalism as opposed to Marxist economics. However, upon observation and recognition of states' interest, Vandevelde concluded that liberalism in this context is limited as it gives the opportunity to host states to pursue their economic nationalist policies.<sup>236</sup> This is indeed a plausible observation. The investment tribunals have taken into account states' justification to legitimise certain regulatory measures when it is necessary for the general interest of the public. This maintains the public feature of investor-state arbitration. Liberalism is confined to the areas specified in the treaties, such as pre-establishment or established investments and the various exceptions in the national treatment provision. The focus of investment treaties is rather to provide investment security or protection in the covered area. This includes the principle of non-discrimination manifested in the national treatment provision.

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<sup>232</sup> Many writings on the history of international economic law highlight this change of economic theory. See Schwarzenberger, 'The Province and Standards of International Economic Law' (n 140).

<sup>233</sup> Schapiro, 'Industrial Revolution' (n 142) 42.

<sup>234</sup> *Ibid* 43.

<sup>235</sup> Kenneth J Vandevelde, 'Political Economy of a Bilateral Investment Treaty, The' (1998) 92 *American Journal of International Law* 621.

<sup>236</sup> *Ibid*.

As noted earlier, the search of the political economy is not confined to the time of promulgation or the historical evolution of the investment regime. It must also reflect the contemporary issues from the role of regulatory states and states' law making capacity, protectionism, democracy, state necessity, public interest, environment and social values to complex investment nature and political risks.<sup>237</sup> It is the observation of this thesis that today's political economy can be looked at from two angles, i.e the creative modern legislations that could potentially hide protectionist agenda; and the multifaceted domestic economic, social and environmental impacts that need investment regulations.

First is from the viewpoint of the protection needed by modern investments against creative legislation that could potentially hide protectionist agenda. States are able to introduce face-neutral-measures that result to discriminatory impact on foreign investors. This form of intervention was not obvious in the past where expropriations were more rampant. It has today become a major concern of investments.<sup>238</sup> This change in the economic indirect intervention is a real challenge in investment arbitration as it is often a difficult task to identify real government intentions behind measures. Investments involve a long span of time in the host states. In certain sectors such as natural resources or infrastructure, the duration would take until the

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<sup>237</sup> Walde made a remark on this,

‘The contemporary situation is one of an acceleration of the globalisation process, of regional and multilateral economic integration, of privatisation, liberalisation and deregulation, of an international environmental and social values export. Issues of non-discriminatory open access and the tension with domestic protectionism, also with environmental and social values (human rights) - in investment similar to the situation in international trade - are the key issues of the agenda of the year 2000.’

See Thomas W Walde, ‘Changing Directions for International Investment Law in the Global Economy An Overview of Selected Issues’ 4-2 CEPMLP Website <<http://www.dundee.ac.uk/cepmlp/journal/html/vol4/article4-2.html>>., <<http://www.dundee.ac.uk/cepmlp/journal/html/vol4/article4-2.html>> , accessed on 29 July 2013.

<sup>238</sup> World Development Report 2005, *A Better Investment Climate for Everyone* (n 7).

project ends or until financial returns are obtained.<sup>239</sup> Such span of time also means that it is exposed more to risks, both economic or political, especially the latter, arising from the change of host states regulations. While economic changes could at times be forecasted<sup>240</sup> and accepted as ordinary business risks to the investors, changes in regulation are normally abrupt and cause devastating impacts on the survival of the investment. The investors fear of the decreasing value of the investments because of host states' actions or regulation.<sup>241</sup> Nationals are more inclined to receive better treatment from their government as compared to foreign investors simply because the government has the power to regulate and domestic interests to protect. Changes in regulation may be affecting any stage of the investment, in the form of increase in taxes, restrictions on the transfer of funds and introductions of conditions or procedural requirements. They may be under the name of environmental regulation, health or public security. The fragility of investments, its financial viability<sup>242</sup> and level playing field are unique natures and needs of investments that the tribunals need to capture when discussing on the impact of government regulatory measures.

Secondly, it is from the angle of host states' interest and the increasing awareness of the effects of liberalism to the domestic economy. At the early stage of the promulgation of investment treaty, it may not be as obvious, as at that time, the states (especially the developing states) more than ever needed foreign investment to

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<sup>239</sup> An aspect that must be understood is the importance of the financial viability of investments. Foreign investors constantly ensure that their investments are financially viable to survive the long term operation in the host state. This is in fact assumed to be the first consideration taken by foreign investors before a decision to invest abroad is made. See Imad A Moosa, *Foreign Direct Investment: Theory, Evidence and Practice* (Palgrave Macmillan 2002) 102.

<sup>240</sup> e.g loss in demands, increase in competition or changes in exchange rates.

<sup>241</sup> See *GAMI Investments, Inc v The Government of the United Mexican States*, Final Award 15 November 2004, para 28.

<sup>242</sup> As compared to international trade, the exporters still have the option to cease exporting if the situation in the host importing country is unfavourable to the product.

build infrastructures and economy. Thirty years later, the effects of such liberalisation is felt, domestic investments especially from the emerging economies are becoming capable but still could not stand the rigorous competition of FDI inflow.<sup>243</sup> Studies have shown that there are signs towards protectionism.<sup>244</sup> Observers have related this to the re-evaluation of the FDI framework and the insertion of exceptions, the global financial crisis and recession.<sup>245</sup> Another interesting recent development that one could relate is the mobilisation of new immigrants which are pushed out of their countries because of economic pressures that hit several European countries.<sup>246</sup> These European immigrants, for instance those from Spain and Portugal are settling in volumes in developing countries or former colonies such as Uruguay and Mozambique. Many have enough capital to set up small investments and are expected to compete the same investment incentives under relevant investment treaties. On a bigger level, the increasing numbers of multinational companies which run big scale investments are effectively causing concerns to states (even developed ones) of the threat they may impose to local industries.<sup>247</sup> There are also real social and environmental issues that the host states

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<sup>243</sup> Leon Trakman, 'Foreign Direct Investment: Hazard or Opportunity?' [2010] University of New South Wales Faculty of Law Research Series 2010 <<http://law.bepress.com/unswwps-flrps10/art32>>, accessed on 28 January 2014.

<sup>244</sup> Sauvant, 'FDI Protectionism Is on the Rise' (n 13); Karl P Sauvant, 'Driving and Countervailing Forces: A Rebalancing of National FDI Policies' in Karl P Sauvant (ed), *Yearbook on International Investment Law & Policy 2008-2009*. (Oxford Univ Pr 2009). See also in the context of trade Matthieu Bussière and others, 'Protectionist Responses to the Crisis: Global Trends and Implications' (2011) 34 *The World Economy* 826.

<sup>245</sup> Sauvant, 'FDI Protectionism Is on the Rise' (n 13).

<sup>246</sup> Robyn Curnow, 'Portuguese Head to Mozambique to Escape Eurozone Crisis' (*CNN*, 15 August 2012) <<http://edition.cnn.com/2012/08/15/business/mozambique-portugal-economy/index.html>> accessed 21 August 2013; 'Argentina, Uruguay Among Region's Most Wanted For Immigration' (*InvestBA.com*, 18 March 2013) <<http://investba.com/2013/03/immigration-to-argentina-and-uruguay/>> accessed 21 August 2013.

<sup>247</sup> An example is the 'Buy American' requirement on foreign investors in the USA. This was challenged in *ADF Inc. v USA*. See attempt to end it via the Trans Pacific Partnership in John Ivison, 'John Ivison: Trans-Pacific Talks Provide Opportunity to Put an End to Buy American Protectionism' (*National Post*, 3 March 2013) <<http://fullcomment.nationalpost.com/2013/03/03/john-ivison-trans-pacific-partnership-talks-provide-opportunity-to-put-an-end-to-buy-american-protectionism/>> accessed 21 August 2013. See also J.D Foster, 'United States International Tax Policy: Tax Neutrality or Investment Protectionism?' (*Tax Foundation*, 10 November 1994), <

have to deal with the influx of foreign investments.<sup>248</sup> It is because of this realisation, that the interpretation of national treatment should accommodate real issues and find the right balance by utilising public administration law tools for more acceptable decisions.<sup>249</sup>

#### **4.0 Likeness Test: The Real Battle in National Treatment**

Like circumstances is integral in the interpretation of national treatment. It is mandated in many investment treaties. The NAFTA Article 1102 for instance literally inserts ‘like circumstances’ in its national treatment provision.

‘Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.’

Even in cases without specifying in like circumstances, it is observed that the assessment should nevertheless be constructed. In the case of *Nykomb v Latvia*, the tribunal asserted that the general test in a discrimination assessment is to examine

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<http://taxfoundation.org/article/united-states-international-tax-policy-tax-neutrality-or-investment-protectionism>>, accessed 21 August 2013.

<sup>248</sup> One example is the question of food security. This is due to masses of land which are under the private ownership of foreign investors for projects like biofuel, irrigation and livestock. There are issues of limited local access to land, food and water and distribution of food to home and host-countries. See Lorenzo Cotula, ‘Land Grab or Development Opportunity? International Farmland Deals in Africa’ in Karl P Sauvart and others (eds), *FDI Perspectives: Issues in International Investment* (2011).

<sup>249</sup> The international investment law literatures are currently heading towards this awareness in search for a more sustainable investment regime. See for instance Benedict Kingsbury and Stephan Schill, ‘Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law’ (Social Science Research Network 2009) SSRN Scholarly Paper ID 1466980 <<http://papers.ssrn.com/abstract=1466980>> accessed 29 April 2013; Stephan W Schill, *International Investment Law and Comparative Public Law* (Oxford University Press 2010).

like with like.<sup>250</sup> This case invoked Article 10 of the ECT which does not contain expressed comparator requirement. Similarly, in the case of *Saluka Investments BV v Czech Republic* which conducted an examination of discrimination under the fair and equitable treatment claim, the tribunal examined the comparable position of the big four banks regarding the bad debt problem – akin to an ‘in like circumstances’ assessment.<sup>251</sup> The OECD commentary on the Draft Multilateral Agreement on Investment (MAI) maintained that the national treatment and most favoured nation treatment by themselves are comparative terms.<sup>252</sup>

As most national treatment provisions are without detailed elaboration,<sup>253</sup> the debate remains on the degree of the protection, or the extent in which the host states are obliged to protect foreign investors or investments. The arbitrations, seen collectively, agree that the interpretation depends on the examination of the context of specific circumstances of each case.<sup>254</sup> This general observation nevertheless loosely allows independent interpretation and opens a wide door to inconsistency. The inconsistency is largely due to the interpretation of likeness.<sup>255</sup>

The difficulty is to determine likeness in the investment setting where there is nearly no physical attributes that can be compared. The comparison is thus upon other contingent attributes of the investment, commonly from the sector of the investments

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<sup>250</sup> *Nykomb Synergetics Technology Holding AB v The Republic of Latvia*, Energy Charter Treaty, Arbitration Institute of the Stockholm Chamber of Commerce, 16 December 2003, page 34.

<sup>251</sup> *Saluka Investments BV v. Czech Republic*, UNCITRAL Arbitration, Partial Award, 17 March 2006, para 314- 323.

<sup>252</sup> This discussion took place in deciding whether ‘in like circumstances’ should be included in the MAI draft. See OECD, ‘The Multilateral Agreement on Investment Commentary to the Consolidated Text’ (n 188) 11.

<sup>253</sup> National treatment is an ambiguous relative right. See Jose E. Alvarez, ‘The Emerging Foreign Direct Investment Regime’ (2005) ASIL Proceedings, (n 155) 95.

<sup>254</sup> *S.D Myers Inc v Canada*, (n 24), para 249.

<sup>255</sup> See the broadness of interpretation in *OEPC v Ecuador* (n 18) as opposed to narrow interpretations in *Feldman v Mexico*, (n 15), *Methanex v USA* (n 19).



and their investment activities. Tribunals have not simplified the criteria or characteristics of likeness for investments. There are however traces or criteria - some commonly invoked by the tribunals and some isolated approaches- that are able to provide a view of the development of this area of jurisprudence. This part attempts to structure these findings and suggest some linkages and observations.

The most prevalent approach in investment tribunals is to determine the economic sector of the comparators.<sup>256</sup> In *Pope & Talbot Inc. v Canada*, the tribunal asserted that as a first step to this analysis, comparison must be made among investments in the same business or economic sector.<sup>257</sup> The tribunal in *Pope & Talbot Inc. v Canada* referred to the OECD analysis on national treatment that as regards to ‘in like situations’, the comparison is valid only if it is made between firms operating in the same sector. The tribunal also took note that the economic sector should not be the only determinative factor, but must take into account the general considerations such as the policy objectives of the member countries.<sup>258</sup> Similarly, in the case of *SD Myers*, the tribunal referred to the OECD practice.<sup>259</sup> In *SD Myers*, the tribunal in comparing between the PCB operators held,

The concept of “like circumstances” invites an examination of whether a non-national investor complaining of less favourable treatment is in the same “sector” as the national investor. The Tribunal takes the view that the word

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<sup>256</sup> See *Methanex v USA* (n 19), *Pope & Talbot Inc. v Canada* (n 20), para 78.

<sup>257</sup> *Pope & Talbot Inc. v Canada* (n 20), para 78. This approach was also adopted in *Parkerings v Lithuania* in determining likeness in most favoured nation claim. See *Parkerings- Compagniet AS v Republic of Lithuania* (ICSID Case No. ARB/05/8), para 371.

<sup>258</sup> *Pope & Talbot, Inc. v Canada*, (n 20), para 78.

<sup>259</sup> *SD Myers, Inc. v Canada*, (n 24), para 248.

“sector” has a wide connotation that includes the concepts of “economic sector” and “business sector”.

However, within the criteria of economic sector, the tribunals have differed as to the narrowness or broadness of the economic activities. In the case of *Feldman v Mexico*, the tribunal has adopted a much narrower application of economic sector, in that it was limited to the reselling and exporting of investments in the cigarette industry.<sup>260</sup> Similarly, in the case of *Methanex v USA* and *UPS v Canada*, the tribunals held that methanol and ethanol investment were not in like circumstances despite both being in the oxygenate market and investments in the postal industry differently. Thus it could be discerned that being in the same economic sector is not the sole and determinative factor of likeness. The tribunals have to take into consideration the policy objectives of the measure that could flip likeness otherwise.

There is no fixed definition of economic sectors which could be imposed in the determination of likeness. A general division of the industrial sector can be seen in statistics done at the international level on foreign direct investment for instance by UNCTAD or OECD.<sup>261</sup> Some examples of sectors are agriculture and fishing, mining and quarrying, food products, metal and mechanical products, construction, trade and repairs, finance and transport and communications.<sup>262</sup> These divisions are

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<sup>260</sup> *Feldman v Mexico*, (n 15), para 171.

<sup>261</sup> Direct Investment by Industrial Sector, International Direct Investment Database, OECD, <[http://stats.oecd.org/Index.aspx?DatasetCode=FDI\\_FLOW\\_INDUSTRY](http://stats.oecd.org/Index.aspx?DatasetCode=FDI_FLOW_INDUSTRY)>, accessed on 28 January 2014. Foreign direct investment in the financial sector - Experiences in Asia, Central and Eastern Europe and Latin America CGFS Publications No 25. June 2005. <<http://www.bis.org/publ/cgfs25.htm>>, accessed on 28 January 2014.

<sup>262</sup> For example, see ‘Morocco Table 5. FDI Flows in the Host Economy, by Industry, 1996-2006 (millions of dirhams)’ World Investment Directory. Volume X Africa. 2008 page 447, <[http://www.unctad.org/en/docs/iteiit20075\\_en.pdf](http://www.unctad.org/en/docs/iteiit20075_en.pdf)>, accessed on 28 January 2014.

general and may only be helpful for the first string filter in the search of likeness.<sup>263</sup>

The examination must proceed further because investment activities tend to specialise. In the wood industry alone, there could be a range of specialisation, such as wood lumbering, moulding, flooring and coating. Investment activities vary depending on factors including the potential profit they can accumulate, skill, demand and resources. In *SD Myers*, the tribunal viewed that ‘sector’ is a wide connotation that includes the concept of economic sector and business sector. The tribunal however did not provide the details of the two concepts, but concluded that SDMI and Myers Canada were in like circumstances with the Canadian operators from the business perspective, because of the same group of customers.<sup>264</sup>

As if the possibility of broad range of activities within an economic sector is not enough, the tribunal in the case of *OEPC v Ecuador* has even widen the application of likeness. Such approach, if taken for the purpose of national treatment will not only hold unnecessary barrier to the host states’ power to legislate but also open a floodgate of discrimination claims. This explains the controversy on the *OEPC v Ecuador* award where companies engaged in exports were considered alike even if encompassing different sectors, including export of petroleum, flowers and seafood

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<sup>263</sup> As there could be a variety of measure of how embracing an economic sector can be, it is best to examine the most obvious, reasonable, practical and recognised specialisation in the area which consist of a handful of players. For instance, it is unlikely to conclude that mining activity and fishing activity should be in the same sector because both involve extraction and production of raw materials. It is also inappropriate to assume a retailing business and a barber shop as alike due to provision of services to consumers. This is taken if the broad division of economic sector is applied, namely primary, manufacturing and service sector. For general reading on FDI and economic sector, see Laura Alfaro. Foreign Direct Investment and Growth: Does the Sector Matter? Harvard Business School . April 2003, <<http://www.people.hbs.edu/lalfaro/fdisectorial.pdf>>, accessed on 28 January 2014.

<sup>264</sup> *S.D. Myers Inc. v Canada*, (n 24), para 250.

products.<sup>265</sup> It was described as ‘diametrically at odds’ when compared to other cases which apply a much narrower approach.<sup>266</sup>

It is not firm whether it is a ‘must’ that investments in like circumstances should be in the same economic sector.<sup>267</sup> What was worrying about the inconsistency between the *OEPC v Ecuador* and other investment cases is not so much on the economic sector factor, but rather the absence of firmer criteria that could be relevant across cases. There is an absence of substance in the *OEPC v Ecuador* decision that could otherwise fill the essence of like circumstances.

Hence, some scholars have suggested the role of competition as a factor of likeness.<sup>268</sup> It is presumed that two investments are considered alike if they are competing with each other. In investments, the investors in the same business will generally strive to gain profit in the same investment climate. This is in line with the purpose of the national treatment provision to ensure foreign investors a level playing field and similar competitive opportunities with the local investments.<sup>269</sup>

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<sup>265</sup> *OEPC v Ecuador*, (n 18), paras 168-173.

<sup>266</sup> This case is often compared to *Methanex v USA* which highlighted differences in the methanol and ethanol industry. Kurtz, ‘The Use and Abuse of WTO Law in Investor-State Arbitration’ (n 40). See also Campbell McLachlan, Laurence Shore and Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (Oxford University Press 2008) 252.

<sup>267</sup> Kurtz suggested that it is a must that likeness is between investments in the same economic sector. See Jurgen Kurtz, ‘Balancing Investor Protection and Regulatory Freedom in Investor-State Arbitration: The Complex Search for State Purpose in a National Treatment Inquiry’ [2012] Institute for International Law and Justice, <<http://www.iilj.org/research/documents/KurtzBalancingInvestorProtectionandRegulatoryFreedomPaper.pdf>>, accessed on 6 October 2013. In the case of *CPI, Inc. v Mexico*, the tribunal regarded that it is ‘necessary’ to begin with the assessment of the same business or economic sector. See *CPI, Inc. v Mexico*, (n 98), para 120. This thesis will however put forth a view that likeness can occur across economic sector if the circumstances permit (so as to contrast with *OEPC v Ecuador*). See further discussion in Ch.6.

<sup>268</sup> Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’ (n 102). See also *UPS v Canada*, Separate Statement of Dean Ronald A. Cass (n 206), para 17.

<sup>269</sup> Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 151.

The discussion over the relevance of competition in investment cases can be seen in the case of *Methanex v USA*. The tribunal did not explicitly rule out its relevance but obviously did not consider it as a basis of likeness either. The argument that likeness should be construed from the viewpoint of competition of the investments was brought by the claimant. The tribunal instead was inclined to reject likeness between the competing investments of methanol and ethanol because of the existence of another methanol investment which was in ‘most’ like circumstances. The rejection of the competition test raises question of what likeness should sensibly be. The rejection was not due to substantiated justifications of the discrimination by the host state but fearing the perverse state of ignoring a more identical methanol producer elsewhere. Similarly, in the case of *UPS v Canada*, *Feldman v Mexico* and *Pope & Talbot*, the tribunals did not construe the obvious competitive situations of the claimants and the comparators. In the case of *UPS v Canada*, the competitive relationship between the investor and the national postal company was not given weight by the tribunal when construing likeness. The tribunal was distracted by more specific differences in the type of service that the investments are operating. Dean Ronald A. Cass dissented the direction of the tribunal and elaborated that;

‘The most natural reading of NAFTA Article 1102, however gives weight to a showing of competition between a complaining investor and an investor of the respondent party in respect of the matters at issue in a NAFTA dispute under Article 1102. Article 1102 focuses on protection of investors and investments against discriminatory treatment. A showing that there is a

competitive relationship and that two investments are similar in that respect establishes a prima facie case of like circumstances.<sup>270</sup>

In a similar vein, the tribunal in the case of *Corn Product International, Inc. v Mexico* acknowledged the role of competition as a basis of likeness. The tribunal held that the High Fructose Corn Syrup (HFCS) tax has altered the terms of competition of the investment products involved. The competitive relationship between HFCS and the domestic sugar has brought to the similar treatment by Mexican law as being interchangeable.<sup>271</sup> In the context of investment law, such competitive relationship is an appropriate indicator of likeness.

In relation to competition, the tribunals had to encounter the relevance of GATT/WTO jurisprudence. The relevance of decided GATT/WTO decisions of the products in question is normally raised by the claimants in the attempt to support their arguments.<sup>272</sup> The *Methanex v USA* tribunal was however mindful that GATT's context is different to investment and was reluctant to adopt the practice in that issue.<sup>273</sup> On the other hand, in *CPI, Inc. v Mexico*, the tribunal acknowledged the relevance of 'like products' test in GATT/WTO to the application of NAFTA Article 1102. The verdict of 'like product' is helpful to determine the nature of the investment involved, even though it does not mean like circumstances.<sup>274</sup> The

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<sup>270</sup> *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, (n 206), para 17.

<sup>271</sup> *CPI, Inc. v Mexico*, (n 98), para 120.

<sup>272</sup> See for instance *CPI, Inc. v Mexico*, (n 98), *Cargill, Inc. v Mexico*, (n 183), *Methanex v USA*, (n 19).

<sup>273</sup> The *Methanex* tribunal was taking a cautionary step in concluding the application of 'like product' in the case. The tribunal however has mentioned earlier in its judgment that due to the similarity in language with GATT Article III, there is a possibility that GATT jurisprudence would assist the tribunal in deciding the case. See *Methanex v USA* (n 19), Part II, Chapter B, para 6. See also reference to *Methanex v USA* in *CPI v Mexico* (n 98), para 123.

<sup>274</sup> *CPI, Inc. v Mexico* (n 98), para 122. The reference of 'like products' in article III of the GATT is inadequate for investment agreements. 'National Treatment' (n 151).

GATT/WTO's experience in national treatment in the 'most authoritative fashion' may provide assistance to international investment.<sup>275</sup>

The conclusiveness of the competition test is another issue. Although it is described as a *prima facie* case of in like circumstances,<sup>276</sup> the tribunals could not turn a blind eye to other factors. The term circumstances must encompass the policy objectives and other relevant criteria. In this regard, the tribunal in the case of *Cargill Inc. v Mexico* held that likeness in the investment products and the competition thereof could not guarantee like circumstances. The tribunal referred to *GAMI v Mexico* and *Pope & Talbot* and asserted that there must be something more than likeness of goods.<sup>277</sup> This is a sensible view as it acknowledged the role of competition but opens the possibility of it being refuted in appropriate circumstances. A comparison can be made to cases which do not regard the relevance of competition at all when it is the most obvious indicator of likeness at the time where other plausible criteria are less convincing.<sup>278</sup>

The scantiness of the competition test to cover all types of investment cases was highlighted by Walde.<sup>279</sup> While competition may indicate likeness, it is not necessary to search for competitiveness of the comparators if it is not relevant to the issue in question. In facing a particular less favourable treatment, it may be more appropriate to industrially compare the investments.<sup>280</sup> In the case of *Nykomb v Latvia*, the

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<sup>275</sup> See Walde, 'In the Arbitration under Article 26 Energy Charter Treaty (ECT), *Nykomb v. The Republic of Latvia*-Legal Opinion' (n 170) , para 39.

<sup>276</sup> *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, (n 206), para 17.

<sup>277</sup> *Cargill, Inc. v Mexico*, (n 183), para 195.

<sup>278</sup> See for instance *Methanex v USA*, (n 19).

<sup>279</sup> Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

<sup>280</sup> The term ' industrial comparability' was introduced in late Prof. Thomas Walde's in his article above. Walde, 'In the Arbitration under Article 26 Energy Charter Treaty (ECT), *Nykomb v. The*

tribunal did not construe the competition test as the industrial characteristics of the comparators were evident. The industrial characteristics considered were the use of same technology i.e co-generation, similar age of construction and similar capacity of production which make both investments fall under the 1995 Entrepreneurial Act. In that case, the comparators were considered in like situation because they were all supplying electricity to Latvenergo and were operating an environment friendly co-generation. The test of likeness in *Nykomb v Latvia* required a look into the technical characteristics of the investments.<sup>281</sup>

The case of *Nykomb v Latvia* also indicates the construction of likeness from the viewpoint of local legislation. Similar host state guarantees may render the investments covered in similar circumstances. Host states guarantee can be in the form of contracts, laws enacted or government circulars of which are relied upon by investors. In *Nykomb v Latvia*, the fact that Windau, Gulbene and Siltums entered into contract with Latvenergo roughly at the same period, the investments were therefore entitled to the same double tariff pursuant to the Entrepreneurial Law 1995.<sup>282</sup>

Similarly, in *CPI, Inc. v Mexico*,<sup>283</sup> the Mexican government made a commitment in writing guaranteeing access to duty-free imported yellow corn for the purpose of producing HFCS in April 1994. Acting in response of that commitment, the joint venture was concluded. However, when the Federal Congress in Mexico enacted a

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*Republic of Latvia-Legal Opinion* (n 170). Competition and its relevance to investment test of likeness will be discussed in depth in Ch.3 and 6.

<sup>281</sup> This was concluded briefly by the tribunal, by inference of the earlier discussions in the award. See *Nykomb v Latvia*, (n 250), 4.3.2 (a), pg34.

<sup>282</sup> *Ibid.*, 3.5.2, pg 16

<sup>283</sup> *CPI Inc.v Mexico*, (n 98), para 28.



legislation which exempt from tax all soft drink manufactured using sweeteners made exclusively from cane sugar, it was as if Mexico has closed off access for HFCS to the soft drinks market because soft drink bottlers switched *en masse* to the use of the untaxed cane sugar as sweeteners.<sup>284</sup> The tribunal concluded that the HFCS tax was a violation of national treatment.<sup>285</sup>

However, some tribunals have disregarded the dynamic criteria of investment nature, operation and management. In the case of *ADF Group Inc v United States of America*, the tribunal did not look at the investment circumstances of the investor as compared to the local comparators.<sup>286</sup> While the US comparators were not affected by the ‘Buy America’ clause - considering that their steel fabrication were originally from and within America, the claimant’s ordinary cause of business of fabricating steel via its subsidiary in Canada was considered against the US law. By fabricating steel within US, it would cause the investment ‘a massive expenditure’ having to manage it in different locations and hiring additional workers, which would be unnecessary if it was to be done via the claimant’s subsidiary in Canada. The tribunal applied the like situation test and plainly asserted that it would be unnatural for investors to fabricate steel abroad while other locals perform it locally. The fact that the foreign investor was not allowed to use its own facility unlike the US investors<sup>287</sup> was a barrier in investment which denied the dynamics of investment and the protective aim of international investment agreements.

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<sup>284</sup> *CPI, Inc. v Mexico*, (n 98), para 51.

<sup>285</sup> *Ibid.*, para 143.

<sup>286</sup> *ADF Group Inc. v USA*, (n 173), para 157.

<sup>287</sup> See Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 186.

The investment cases so far have not emphasised directly and explicitly the issue of different economic competencies of investments, but it is a potentially important criterion. An investment with limited use of technology could not be considered alike with a full-tech investment which is able to produce bigger volume of production. An investment with many years of experience and expertise should not be compared with a new investment with limited expertise. As far as small businesses are concerned, it is generally observed they are vulnerable and are more likely to close operation.<sup>288</sup>

One may argue that if such a criterion is undertaken, investments will always tend to differ and the national treatment provision will not serve its purpose. Disadvantaged investments of technology, scale, expertise and financial cap thus needs stronger investment support to keep them running. Due to the open nature of investment opportunities in the world today, it becomes inevitable that small enterprises and big multinational corporations meet. These different entities portray different levels of technical advances and financial strength but are nevertheless expected to compete in the same investment setting. This reality of inequality has urged states to support these industries until they are matured enough to compete internationally.

There are at least two cases that may be indicative towards this direction. This was not declared as a rule but could be accepted by the tribunals depending on the rational of such distinction. In *Parkerings v Lithuania*, the size of the project of Pinus Proprius and BP was taken into consideration.<sup>289</sup> Although the investments were not viewed in terms of operative equality, the tribunal took cognizance that the

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<sup>288</sup> Graham Bannock, *The Economics and Management of Small Business: An International Perspective* (Routledge 2005) 1.

<sup>289</sup> *Parkerings v Lithuania*, (n 257), para 396.

different scale of project should not be taken as in like circumstances. In another case, *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, the tribunal took into account the experience and expertise of the local investor as compared to the foreign investors in the same project.<sup>290</sup>

The examination of likeness includes the broader circumstances of the investors in question. This suggests that two investments should not be regarded as in the same circumstances despite identical physical attribution to the investments because of a broader dispute between the host state and the investor state. There are at least two investment cases that have considered the broader dispute as a factor in determining likeness. In the case of *Pope & Talbot v Canada*, the tribunal agreed that the legal context in determining likeness includes the entire background of the dispute between Canada and the United States concerning softwood lumber trade.<sup>291</sup> The tribunal saw that the underlying economics of softwood lumber industry in Canada made the comparators unlike and that the new entrant's allocation choice by Canada had a reasonable nexus with a rational and non-discriminatory policy.<sup>292</sup> In the other case of *CPI, Inc. v Mexico*, the discrimination was a countermeasure to a broader dispute between US and Mexico on the ban of Mexican sugar cane products. The tribunal did not however take into account the Mexican denied access to the US market and concluded that the comparators are adequately alike for the purpose of Article 1102.<sup>293</sup>

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<sup>290</sup> *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan* (hereinafter '*Bayindir v Pakistan*') ICSID Case No. ARB/03/29, Award, 27 August 2009, para 410.

<sup>291</sup> *Pope & Talbot*, (n 20), para 77, p.34.

<sup>292</sup> *Ibid.*, para 93, p41.

<sup>293</sup> *CPI Inc. v Mexico*, (n 98), para 129.

The assessment of likeness as analysed above is factual dependant. The tribunal have taken into consideration several factors, i.e the economic sector, competition, industrial comparability, operative equality, guarantee by host state and broader dispute or circumstances. The tribunals have however done so independently, often ignoring other aspects of likeness while highlighting another. There is a need for a systematic assessment of the criteria of likeness which is the driving motivation of this thesis.

## 6.0 Legitimate Regulatory Measures

A typical national treatment clause in investment treaties generally textually requires two matters; firstly whether there is less favourable treatment and secondly whether the comparators are in like circumstances.<sup>294</sup> A literal reading of the national treatment provision would conclude suffice the findings of the two requirements. In *Thunderbird v Mexico*, the tribunal in responding (albeit indirectly) to the three-part test proposed by the claimant, asserted that the finding of national treatment must follow the plain wording of the text. The obligation of the host state is to accord non-discriminatory treatment to foreign investors. The tribunal held that the claimant must show firstly, whether there was less favourable treatment and secondly whether the investments were in like circumstance.<sup>295</sup>

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<sup>294</sup> The extraction of these two matters can be seen for instance from article 1102 of NAFTA:

‘Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.’

<sup>295</sup> *Thunderbird Case*, (n 199) paras 175-176. This case did not proceed beyond the finding of less favourable treatment and thus it could not be further ascertained as to how the tribunal would or would not construe the justification of the measure as part of its assessment.

To the exception of some investment treaties that provide for the general exceptions which are applicable in the national treatment assessment, investment awards generally considered the assessment of justification as part of the analysis of national treatment. The analysis of the legitimacy of the regulatory measure is rather judicially developed in the investment disputes. The tribunals have not outlined explicitly this methodology, but it can be inferred from its construction and its responses to the more explicit assertions by the disputing parties. The case of *Pope & Talbot, Inc. v Canada* is often referred to in cases and scholarly writings in reference to the examination of legitimate regulatory measure as the third test in a national treatment assessment. The tribunal in its award mentioned:

‘Differences will presumptively violate Article 1102(2), unless they have a reasonable nexus to rational government policies that (1) do not distinguish, on their face or de facto, between foreign owned and domestic companies, and (2) do not otherwise unduly undermine the investment liberalizing objectives of NAFTA.’<sup>296</sup>

This was further highlighted in the subsequent paragraphs that the tribunal would construe the reasonable nexus between the measure and a rational, non-discriminatory government policy if the parties use the substance of an agreement or

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<sup>296</sup> *Pope & Talbot, Inc. v Canada*, (n 20), paras 31-104. Despite the reference to the case of *Pope & Talbot* in relation to the three steps involved, a close reading of the case would reveal that the likeness test and the reasonable nexus between the measure and a rational non-discriminatory policy are not clearly demarcated. The three steps may or may not be independent to each other depending on the facts of the case. The second and third tests are conducted in a merged manner. This observation will be discussed in detail in Chapters 5 and 6 of this thesis. Generally, the three pronged test is deduced by scholars from the approach of the tribunals in construing national treatment assessments. See in particular Weiler, ‘Saving Oscar Chin: Non-Discrimination in International Investment Law’ (n 110); Weiler, *The Interpretation of International Investment Law: Equality, Discrimination, and Minimum Standards of Treatment in Historical Context* (n 135) 447.

measure as an unchallengeable basis for discrimination.<sup>297</sup> In *Parkerings v Lithuania*, the tribunal asserted,

‘However, the situation of the two investors will not be in *like circumstances* if a justification of the different treatment is established.’<sup>298</sup>

The importance of rational or justification can be regarded as inherent in a discrimination assessment. For instance, elsewhere in the case of *Saluka Investments BV v The Czech Republic* which invoked discrimination under a broad fair and equitable treatment provision, the tribunal construed a systematic assessment of comparable situation of the banks, differential treatment and the assessment of lack of justification.<sup>299</sup>

One obvious feature in international investment law is the absence of the expressed general exceptions of the obligations in the international investment agreements. The tribunals however, directed by reasons and common practice in other experienced jurisprudence such as GATT/WTO, have undertaken the examination of whether the host states have the legitimate reasons justifying the discriminatory measure. In the case of *Feldman* the tribunal asserted that:

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<sup>297</sup> *Pope & Talbot, Inc. v Canada*, (n 20), para 81.

<sup>298</sup> *Parkerings v Lithuania*, (n 257), para 375.

<sup>299</sup> See *Saluka Investments BV v The Czech Republic*, (n 251), para 313. The case was concerning Article 3 of the Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of The Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 199. The provision involved is worded as below:

‘Each Contracting Party shall ensure fair and equitable treatment to the investments of investors of the other Contracting Party and shall not impair, by unreasonable or discriminatory measures, the operation, management, maintenance, use, enjoyment or disposal thereof by those investors.’

“In the investment context, the concept of discrimination has been defined to imply unreasonable distinctions between foreign and domestic investors in like circumstances.”<sup>300</sup>

Every discriminatory measure must have reasonable nexus to a rational, non-discriminatory government or international policy.<sup>301</sup> The question of the legitimacy of a discriminatory measure is determinative on whether two investments are in like circumstances, if the latter is construed from the legislative point of view.<sup>302</sup> Thus in investment cases, the tribunals construed this question in two instances, firstly together with likeness in determining appropriate comparators and secondly, as a third step to determine whether the discriminatory measure is justified. A detailed discussion on the plausibility of these approaches will be in Chapter Six under the independent or merged justification test.

The approach taken by tribunals is on a case by case basis and the exceptions and test of reasonableness are derived from various sources and analogy. In the reading of national treatment, there is a minimum presumption that it condones distortions and discrimination and promotes public and environmental protection, as understood across international economic law where national treatment is more familiar.<sup>303</sup> It is thus not surprising if GATT/WTO is referred to or incorporated into the interpretation of national treatment and investment treaties.<sup>304</sup> The approach taken in the case of *SD Myers, Inc. v Canada* is an example of placing the scope of national

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<sup>300</sup> *Feldman v Mexico*, (n 15), para 170.

<sup>301</sup> *Pope & Talbot*, (n 20), para 81.

<sup>302</sup> *Ibid.*, paras 75-76.

<sup>303</sup> Alvarez, mentions that the WTO jurisprudence contains similar principles, hence the presumption. See Jose E. Alvarez, 'The Emerging Foreign Direct Investment Regime', (n 155).

<sup>304</sup> Subedi, *International Investment Law: Reconciling Policy and Principle* (n 27) 187.

treatment in the existence of an environmental concern. Although there is no clear exception that excludes environmental regulations from being challenged by investors, the tribunals seemed to be aware that it deserves cautionary examination. The conclusion so far is that not all environmental regulations are legitimate, as it must be reasonably invoked in the absence of other alternatives. Damage caused to investors because of environmental regulations must only be when it is necessary.

In the case of *SD Myers Inc. v Canada*, the tribunal took note of the approach by GATT/WTO which referred to Article XX (General Exceptions) in the attempt to read the overall legal context of national treatment. In exercising the same approach, the tribunal noted the NAFTA companion agreement NAAEC which provides for the establishment of high levels of environmental protection by states. This allowed a further examination of whether the less favourable treatment of the like investments was justified by legitimate public policy measures, pursued in a reasonable manner. By reasonableness, the tribunal also highlighted the need to avoid trade distortions that are not justified by environmental concerns. The tribunal found that Canada's action was not motivated genuinely by environmental concerns but rather by indirect protectionist motive to maintain the future ability to process PCBs within Canada. As there were a number of legitimate ways that Canada could do to achieve its motive, the prevention of SDMI from exporting PCBs for processing in the USA was unreasonable and a breach of Article 1102 NAFTA.<sup>305</sup>

This scope of application provides space to the host government in exercising their sovereignty in regulation. The OECD Declaration has also mentioned that

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<sup>305</sup> *SD Myers, Inc. v Canada*, (n 24), paras 246-257.



investments must be consistent with the maintenance of public order, the security interest of the host states and international peace and order. They are collectively meant to provide flexibility in the interpretation of the national treatment obligation by allowing reasonable and legitimate regulatory measures.<sup>306</sup>

The reasonableness test in the context of investment must be able to produce a balanced and ideal application of national treatment. The national treatment principle must provide clear and predictable scope of protection to the investors while allowing host states to pursue its national interest. In the past cases, host states were alleged to introduce discriminatory measures that affect foreign investors under the rationales such as for environment protection,<sup>307</sup> national security<sup>308</sup> and economic countermeasure.<sup>309</sup> An observation by UNCTAD has also revealed that many regulatory changes have occurred among countries that has made the investment framework less welcoming.<sup>310</sup> As for the foreign investors, this trend is worrying because host states may drastically change the regulatory set up that is legitimately relied upon by foreign investors.<sup>311</sup>

The tribunal in the case of *Occidental v Ecuador* has stretched the likeness test to include investors across different economic sectors in the view of protection towards

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<sup>306</sup> UNCTAD recognises the ‘economic asymmetry’ that require a degree of flexibility of national treatment especially in developing countries. See UNCTAD “National Treatment” UNCTAD/ITE/IIT/11 (Vol.IV) p 2.

<sup>307</sup> *SD Myers, Inc. v Canada*, (n 24), *Methanex v USA*, (n 19).

<sup>308</sup> For better control over tax revenue, discourage smuggling, protection of intellectual property and prohibition of grey market sales. See *Feldman v Mexico*, (n 15), para 176.

<sup>309</sup> *CPI Inc. v Mexico*, (n 98).

<sup>310</sup> World Development Report 2005, *A Better Investment Climate for Everyone* (n 7). See also Sauvart, ‘FDI Protectionism Is on the Rise’ (n 13).

<sup>311</sup> On environmental regulation, see Waelde and Kolo, ‘Environmental Regulation, Investment Protection and “Regulatory Taking” in International Law’ (n 39) 819.

foreign investors but failed to explain the reasonableness of doing so.<sup>312</sup> In *UPS v Canada*, the tribunal failed to examine the reasonableness on an acceptable threshold to prove why two investments are not in like circumstances when they are in obvious competition and in the same economic sector.<sup>313</sup>

The reasonableness of the ‘Buy America’ measures was also not discussed by the tribunal in *ADF Group Inc v America*. The tribunal rejected the claim because the investor failed to identify a US steel manufacturer or fabricator which was treated differently.<sup>314</sup> The search for a comparator as required by the tribunal is almost impossible because a local investor would not possibly fabricate steel abroad, unlike the foreign investor which has parts of its facilities in its home state. The examination of likeness should not necessarily be confined to the physical location of the facilities, but could be viewed from another account such as the freedom of using the investment’s own facilities regardless the location.<sup>315</sup> As such it is plausible to examine the reasonableness of the measure especially its impact on an investment. In responding to the respondent’s allegation that the investor’s claim was a claim relating to ‘goods’ not ‘investment’, the tribunal mentioned:

‘Those areas include “management, conduct and operation” of a Canadian “enterprise” in the US and the goods produced by such enterprise in the territory of the US can be regarded as investments of the Canadian investor

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<sup>312</sup> *OEPC v Ecuador*, (n 18), para 173.

<sup>313</sup> *UPS v Canada*, Separate Statement of Dean Ronald A. Cass (n 21), para 17.

<sup>314</sup> *ADF Group Inc. v USA* (n 173), paras 156-7.

<sup>315</sup> The same view has been mentioned in Andrew Newcombe, see Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 7) 185.

and are closely related to , and are the results of, the “management, conduct and operation” of the enterprise<sup>316</sup>

The exception under the ground of national interest is not fully developed in national treatment jurisprudence. However, there are indicators by UNCTAD that host states are increasingly exploiting gaps in the international regime to introduce protectionist measures and invoking the justification of ‘national security’ or ‘interest’. Among potential areas are favouring products with high domestic contents in government projects, subsidy like incentives for domestic investors and barriers on products which may affect investments.<sup>317</sup> It is predicted that more protectionist measures will be introduced, testing the doctrine of national treatment to its full capacity.

#### **4.0 Conclusion**

Based on the existing cases, this chapter has attempted to draw the pattern of interpretation of the national treatment principle in international investment cases. The appreciation of the objectives, scope and features of the national treatment principle is crucial in order to result in a directed and contextual interpretation and application of the doctrine. This provides the framework of the sub-tests on determination of likeness and reasonableness that builds up the substantive reasoning of the tribunals. Accompanied by the acknowledgment of the distinctive nature of investments and how investments are affected by a government measure, the

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<sup>316</sup> *ADF Group Inc v America*, (n 173), para 155.

<sup>317</sup> ‘Investment Policy Developments in G-20 Countries’ (United Nations Conference on Trade and Development 2009). <[http://unctad.org/en/Docs/webdiaeia20099\\_en.pdf](http://unctad.org/en/Docs/webdiaeia20099_en.pdf)>, accessed on 21 August 2013.

tribunals should be able to understand the situations of investments and assess likeness therefrom.

The observations in this chapter are not conclusive as this research will continue to study similar protections under the GATT/WTO, European Union Law and International Human Rights law and derive possible methods and analogies that can be transposed in international investment law. It has however laid an important foundation for the comparisons to take place.

## Chapter 3

### RELEVANCE OF GATT/WTO DOCTRINE OF NATIONAL TREATMENT TO INTERNATIONAL INVESTMENT LAW

#### 1.0 Introduction

The interaction of trade and investments are interwoven in the practical world, but the legal structure which governs both areas is fragmented.<sup>318</sup> The point of similarity between these separate fields of laws is the non-discrimination principle, manifested in the national treatment and most favoured nation provisions. The key issue in this chapter is to determine whether the interpretation of national treatment in trade could provide interpretative guidance to international investment law. To attempt this question, this thesis firstly lays the foundation of comparison; beginning with the underlying philosophies of trade and investment followed by the basis of comparison of the national treatment principle in both jurisprudences. It will then look at the various incorporations of national treatment provisions in the WTO texts and explain the relevance of GATT as the major comparison.

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<sup>318</sup> Mary E Footer, 'On the Laws of Attraction: Examining the Relationship Between Foreign Investment and International Trade' in Roberto Echandi and Pierre Sauve (eds), *Prospects in International Investment Law and Policy* (Cambridge University Press 2013) <[http://www.cambridge.org/us/knowledge/isbn/item7113132/?site\\_locale=en\\_US](http://www.cambridge.org/us/knowledge/isbn/item7113132/?site_locale=en_US)>, accessed on 12 June 2013; T. Broude, 'Investment and Trade: The "Lottie and Lisa" of International Economic Law?' (2011) 8 Transnational Dispute Management (TDM) <<http://www.transnational-dispute-management.com/article.asp?key=1741>>, accessed on 28 January 2014.

The primary part of this chapter is to examine the analysis of likeness in the GATT/WTO jurisprudence and to see what lessons that could be learnt. As will be further developed in this chapter, it is concluded that the GATT/WTO jurisprudence is highly instructive especially in assimilating the economic context of the interpretation of likeness. This is achieved by highlighting the competitive relationships between the comparators. This is apt, considering that the investment treaties are economic legal instruments. This would be in line with the contextual interpretation as required in Article 31(3)(c) of the Vienna Convention of the Law of Treaties (VCLT). Thus, in so doing, this chapter will examine references to GATT/WTO in the investment decisions, the view of the scholars on its acceptance and rejection, and the suitability of the relevant tests of likeness in GATT/WTO namely; the traditional physical characteristic approach, the aims and effect test, directly competitive or substitutable approach (DCS) and the product process doctrine.

The last section of this thesis is dedicated to the finding of legitimate regulatory measures. The intrinsic difference as highlighted by many scholars is the absence of an exception provision similar to Article XX of GATT/WTO.<sup>319</sup> This thesis finds interesting lessons, in particular the use of the *chapeau* which resembles the proportionality test that needs to be further propagated in international investment law. It also highlights the methodological need for flexibility in applying both the three prong test and merged justification test as an after effect of the incorporation of a similar Article XX GATT/WTO exception in investment treaties.

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<sup>319</sup> Barton Legum and Ioana Petculescu, 'GATT Article XX and International Investment Law' in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013); Kurtz, 'The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO' (n 102).

This chapter generally supports the comparative exercise towards coherence (though not necessarily full convergence),<sup>320</sup> the proliferation of the rule of law in the application of the non-discrimination principle<sup>321</sup> and the development of international investment law which takes into account the experience of other jurisprudences with similar questions.<sup>322</sup>

## 2.0 The Underlying Philosophy of GATT/WTO: A Comparison to Investment

The entire philosophy of GATT stems from the idea of liberalisation.<sup>323</sup> Liberalisation was promulgated following the collapse of the international economy after the World War I which was aggravated by trade restrictions and protectionist measures.<sup>324</sup> It was a worldwide traumatic experience of the 1920s and 1930s that

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<sup>320</sup> Broude used the term ‘consolidation’. A cautioned view could be seen in Tietje in that the merge would overburden the systems. This thesis agrees that this comparison is not to call for a merger but rather coherence in the general development of international economic law. See T. Broude, ‘Investment and Trade’ (n 318); Christian Tietje, ‘Perspectives on the Interaction between International Trade and Investment Regulation’ in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013). See also JHH Weiler, ‘Cain and Abel- Convergence and Divergence in International Trade Law’, *The EU, the WTO and the NAFTA: Towards a Common Law of International Trade? (Lindahl Lectures)* (Oxford University Press, USA 2000).

<sup>321</sup> Tietje, ‘Perspectives on the Interaction between International Trade and Investment Regulation’ (n 320).

<sup>322</sup> Anthea Roberts, ‘Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System’ [2013] 107 *American Journal of International Law*.

<sup>323</sup> Alan O. Sykes, ‘Protectionism As a Safeguard: A Positive Analysis of the GATT Escape Clause with Normative Speculations’ (1991) 58 *University of Chicago Law Review* 255.

<sup>324</sup> The controversial U.S Hawley –Smoot Tariff in 1930 was an example of high tariff set by the Republicans in power and was later reduced by the Democrats. Although the tariff was not a direct causation to the Great Depression, it had caused to a drop of domestic imports and further led to other symmetric effects including the ‘inability of foreign countries to earn dollars from exports to United States’ and higher trade barriers which aggravated the international tension. Douglas A Irwin, ‘From Smoot-Hawley to Reciprocal Trade Agreements: Changing the Course of U.S. Trade Policy in the 1930s’ in Michael D Bordo, Claudia Dale Goldin and Eugene Nelson White (eds), *The Defining Moment: The Great Depression and the American Economy in the Twentieth Century* (University of Chicago Press 1997) 336. See also Robert E Hudec, ‘Circumventing Democracy: The Political Morality of Trade Negotiations’ (1992) 25 *New York University Journal of International Law and Politics* 311, 313.; Bussière, Pérez Barreiro, Straub, and Taglioni, ‘Protectionist Responses to the Crisis’ (n 244).

discouraged international trade.<sup>325</sup> States felt the urge to revert to the pre-war I economic conditions.<sup>326</sup> It was a difficult setting in the 1930s having to face with the rise and threat of fascism, that the democratic bloc gathered effort towards international cooperation in trade and finance by ending unregulated protectionism. By the removal of trade barriers and protectionist measures, states were able to trade liberally in the view that it would enhance the economic condition and the living standards of the people. This led to the negotiation of GATT which clearly enunciated the motivation to enhance the economic and living standard by liberating trade.<sup>327</sup> The preamble reads,

‘Recognizing that their relations in the field of trade and economic endeavour should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, developing the full use of the resources of the world and expanding the production and exchange of goods.’<sup>328</sup>

The preamble confirmed the recognition of the benefits of liberalisation in trade by way of efficiency of trade and production popularly put forth in the theories of absolute and comparative advantage.<sup>329</sup> In order to materialise the theory and the

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<sup>325</sup> Douglas A Irwin, Petros C Mavroidis and Alan O Sykes, *The Genesis of the GATT* (Cambridge University Press 2008) 5. The other concern was the failure of the monetary system.

<sup>326</sup> Great Britain and France were the largest foreign investors prior the First World War where commodities and people were able to move freely and on adherence to the international gold standard. See Cameron and Neal, *A Concise Economic History of the World* (n 53) 284–289.

<sup>327</sup> The philosophy of liberal trade is related to the theory of comparative advantage which promotes beneficial specialization, economic growth and higher standards of living. OECD, ‘Trade Principles and Concepts’ (Organisation for Economic Co-operation and Development 1995) OCDE/GD(95)141 5, < [http://ec.europa.eu/environment/integration/pdf/oecd\\_te\\_1995.pdf](http://ec.europa.eu/environment/integration/pdf/oecd_te_1995.pdf)>, accessed on 5 October 2013.

<sup>328</sup> GATT 1947, Preamble.

<sup>329</sup> Adam Smith, *Wealth of Nations* (Prometheus Books 1991); David Ricardo, *On the Principles of Political Economy, and Taxation* (John Murray 1821); John Aldrich, ‘The Discovery of Comparative



benefits accruing to it, it required a move towards liberalisation, again pledged in the preamble that it can be achieved by ‘substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce’.<sup>330</sup> GATT was an outcome of reciprocity of states in order to agree to remove trade restrictions against the protectionist background at that time.<sup>331</sup>

Considering that the whole aim is towards liberalisation, it is not surprising that protectionism is casted as a contrasting element.<sup>332</sup> This is evidenced in the prohibition of protectionism in the GATT in Article III(1). Article III(1) prohibits internal taxation and regulation on imported or domestic products ‘so as to afford protection to domestic production’. GATT functions as a safeguard to the tariff reduction negotiations made among the countries. It survived the International Trade Organization (also referred to as the Havana Charter) and is maintained under the new WTO. The WTO regarded GATT as a ‘past *liberalisation* effort’ in its preamble. It continues to serve as the spinal trade regulating instrument together with other newly introduced texts in the Marrakesh Agreement to what is called as the post war ‘new protectionism’ in the form of non-tariff barriers (NTB).<sup>333</sup> It is gathered from the whole structure of GATT and WTO that it aims to ‘secure

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Advantage’ (2004) 26 *Journal of the History of Economic Thought* 379, 379–399; Cameron and Neal, *A Concise Economic History of the World* (n 53) 276.

<sup>330</sup> GATT 1947, Preamble.

<sup>331</sup> The importance of reciprocity is explained by Trebilcock and Fishbein as opposed to unilateral liberalisation as a refinement of the classical trade theory. Pauwelyn also recognised the ‘reality’ that made it impossible for states to liberalise unilaterally. See Michael Trebilcock and Michael Fishbein, ‘International Trade: Barrier to Trade’ in Andrew T Guzmán and AO Sykes (eds), *Research Handbook in International Economic Law* (Edward Elgar Publishing 2007) 4; Joost Pauwelyn, ‘Transformation of World Trade, The’ (2005) 104 *Michigan Law Review* 1, 10.

<sup>332</sup> Alan O Sykes, ‘Protectionism As a Safeguard: A Positive Analysis of the GATT Escape Clause with Normative Speculations’ (1991) 58 *University of Chicago Law Review* 255; Alan O Sykes, ‘Regulatory Protectionism and the Law of International Trade’ (1999) 66 *University of Chicago Law Review* 1, 1.

<sup>333</sup> Dominick Salvatore, ‘Protectionism and World Welfare: Introduction’, *Protectionism and World Welfare* (Cambridge University Press 1993) 3.

liberalisation'. The effort to secure liberalisation continues in subsequent negotiation rounds to obtain freer trade.<sup>334</sup>

As a point of discussion, the question is, are investment treaties equally aimed for liberalisation? To answer this question, it is helpful to begin at looking at the preambles of investment treaties. The investment treaties are generally entitled 'promotion and protection' or 'encouragement and protection' and the contents are built up towards this aim.<sup>335</sup> The historical evolution of investment treaties also suggests that investment treaties were motivated by the aim to protect citizens' property in a foreign country. One could reasonably and appropriately infer that investment treaties are primarily aimed at protection of foreign investments.<sup>336</sup>

However, a broader assessment of the regime would indicate that investment treaties are also associated to liberalisation.<sup>337</sup> The protection accorded to investments gives a liberalisation effect. Investments also enjoy liberalisation as a result of the protection depending on the scope of the investment treaties, i.e whether they include established or pre-establishment stage or certain economic sectors.

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<sup>334</sup> The Uruguay Round was a prolonged and persistent negotiation towards further liberalisation. The next negotiation was the Doha Round which aimed to achieve liberalisation in agriculture. John Croome, *Reshaping the World Trading System: A History of the Uruguay Round* (DIANE Publishing 1995); Sungjoon Cho, 'Demise of Development in the Doha Round Negotiations, The' (2009) 45 Texas International Law Journal 573.

<sup>335</sup> See for instance US-Latvia BIT (1995) entitling 'encouragement and reciprocal protection of investment' at <[http://unctad.org/sections/dite/ia/docs/bits/us\\_latvia.pdf](http://unctad.org/sections/dite/ia/docs/bits/us_latvia.pdf)>, accessed on 27 August 2013. See also Croatia-Sweden BIT (2000) which contains in its preamble 'promotion and reciprocal protection of investments', at <[http://unctad.org/sections/dite/ia/docs/bits/croatia\\_sweden.pdf](http://unctad.org/sections/dite/ia/docs/bits/croatia_sweden.pdf)>, accessed on 27 August 2013. The important features generally found in the investment treaties which guarantee protection to foreign investors are compensation for expropriated investments, national and most favoured nation treatment, full protection and security and fair and equitable treatment sealed with the right to recourse in international arbitration.

<sup>336</sup> A further discussion of the underlying philosophy of investment treaties to provide protection to foreign investors is elaborated in Ch.2.

<sup>337</sup> Kenneth J Vandeveld, 'Sustainable Liberalism and the International Investment Regime' (1997) 19 Michigan Journal of International Law 373; Vandeveld, 'Political Economy of a Bilateral Investment Treaty, The' (n 235); Kenneth J Vandeveld, 'Economics of Bilateral Investment Treaties, The' (2000) 41 Harvard International Law Journal 469.

Along this line, one could also argue that the trend in today's investment treaties is shifted towards more liberalisation effect. There are investment treaties that are explicit in liberalisation as enshrined in their titles.<sup>338</sup> There are also an increasing number of investment treaties and free trade agreements with investment chapters that provide for national treatment at the pre-establishment stage. The 2004 Canadian FIPAs, 2004 US Model treaties, NAFTA and CAFTA are of this feature.<sup>339</sup> The German Model BITs which constitute a large portion of the world investment treaties also gives the right of foreign investors to access the German markets.<sup>340</sup>

Both the trade and investments treaties are agents of liberalisation, the former aims for it, while the latter plays a contributory role. The only caution related to liberalisation and the interpretation of national treatment stems generally on the possibility that an over-emphasised assessment of liberalisation aim in investment treaties would result to a stretch of pro-investment interpretation of investment substantive provisions, more than investment- protection-aimed investment treaties would.<sup>341</sup> This thesis suggests that both liberalisation and protection aims are not

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<sup>338</sup> See Japanese BITs, for instance Japan-Laos BIT 2008. The title of the agreement mentions 'liberalisation, promotion and protection of investment'. Japan-Laos BIT 2008, <[http://unctad.org/sections/dite/ia/docs/bits/Japan\\_Laos.pdf](http://unctad.org/sections/dite/ia/docs/bits/Japan_Laos.pdf)>, accessed on 20 August 2013. It is similarly worded in the Korea-Japan BIT 2002, <[http://unctad.org/sections/dite/ia/docs/bits/korea\\_japan.pdf](http://unctad.org/sections/dite/ia/docs/bits/korea_japan.pdf)>, accessed on 20 August 2013. In regards of investment treaties of this nature (having both protection and liberalisation aims), Marino Baldi has expressed his reservation as to their effectiveness. See Baldi, 'Less May be More: the Need for Moderation in International Investment Law' (n 51).

<sup>339</sup> See elaboration on pre-establishment national treatment provisions in Ch.2.

<sup>340</sup> Otto Sandrock, 'The Right of Foreign Investors to Access German Markets: The Meaning of Article 2(1) of the German Model Treaty for the Promotion and Protection of Foreign Investments' (2010) 25 ICSID Review 268.

<sup>341</sup> This thesis thus exercise caution in using the word liberalisation so as not to be referred as the aim of investment treaties. Liberalisation in the context of discussion is 'liberalisation of investment' as compared to the 'liberalisation of trade' in the WTO law. It means the reduction of barriers or stringent rules that brings effect to the expansion of investment opportunities. Some writings refer liberalisation to liberalisation of (mere) regulatory framework, while in others it is loosely used together with protection without emphasising on the consequences following it. Vandevelde stated

contradictory but differ only as to the orientation of importance, in which investment treaties primarily prioritise protection more than liberalisation.<sup>342</sup>

An obvious impact that is related to the concept of liberalisation is that it provides a clear justification to combat protectionism. The GATT/WTO has made it even more explicit as a purposive direction of the national treatment provision in Article III(1). Even though such explicit indication is absent in investment treaties, it could be logically inferred that the aim of protection equally denounces protectionism. Protection of investments also means to protect them against protectionism. The protection of investments in the context of the national treatment provision ensures a level playing field between investors in competing investment opportunities. There is economic logic in the need of protection against protectionist measures which are faced similarly by both traders and investors.

The next important similarity in the underlying philosophy of trade and investment is the maintenance of the principles of justice and the rule of law in the prohibition of

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that 'BITs advertised themselves as instruments of liberalization, i.e, instruments for the facilitation and protection of international investment flows'. See Kenneth J Vandeveld, 'Investment Liberalization and Economic Development: The Role of Bilateral Investment Treaties' (1998) 36 Columbia Journal of Transnational Law 501, 503. If liberalisation is taken as the aim of investment treaties, it would mean that all measures introduced by host states must undertake not to defeat the purpose of liberalisation. It would cast greater impact on investments as compared to liberalisation in trade as trade only involves the movements of goods and services which do not have eternal impact on the manufacturing based outside the importing countries and less regulatory measures. On the other hand in investments, liberalisation allows the presence of foreign investments/ investors operating equally and enjoying greater protection than the domestic industry which means that more regulatory measures are exposed to breach of investment treaties.

<sup>342</sup> The historical assessment of investment treaties would also reveal that the main drive for the introduction of the treaties was the lack of protection for foreign investors. In the same vein, Christian Tietje marked that 'modern investment law has, in contrast to trade law, has been developed because of the shortcomings of traditional public international with regard to the protection of interest of private economic actors.' See Tietje, 'Perspectives on the Interaction between International Trade and Investment Regulation' (n 320).

discrimination.<sup>343</sup> Without the national treatment provision in both jurisprudences, investors and foreign goods are exposed to certain discrimination.<sup>344</sup> This would tilt the level playing field and flaw the competitive environment of investments and trade. Although the maintenance of rule of law is relatively needed more by the investors than trade (considering the physical presence of investment in the host state, the obsolescing bargain and the weaker status of the foreign investors), the GATT/WTO is more protective to imported goods. This is ascertained from the more certain approach in highlighting the role of competition as the catalyst of likeness in national treatment. It lifts the assessment to have some economic basis relevant to the interpretation of GATT/WTO and investment treaties which are economic based international legal instruments.

Thus, at least in the underlying philosophy of national treatment in GATT/WTO and investment treaties, disciplining states against protectionism and the emphasis on competition constitute significant grounds of similarity that would justify guidance by way of interpretative context for investor-state arbitration.<sup>345</sup> Both are aimed at

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<sup>343</sup> Ernst-Ulrich Petersmann, 'International Rule of Law and Constitutional Justice in International Investment Law and Arbitration' (2009) 16 *Indiana Journal of Global Legal Studies* 513 (2009) <<http://www.repository.law.indiana.edu/ijgls/vol16/iss2/6>>, accessed on 14 October 2013.

<sup>344</sup> In the context of investment, see Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3). Whereas, in the trade context, see Ernst-Ulrich Petersmann, 'Why Rational Choice Theory Requires a Multilevel Constitutional Approach to International Economic Law - A Response to the Case Against Reforming the WTO Enforcement Mechanism' (2008) 2008 *University of Illinois Law Review* 360. Both literatures suggest the importance of external discipline to complement national constitutionalism in an increasing globalising world based on principles of justice which includes the non-discrimination principle. In line with this, see also Jan Paulsson, *Denial of Justice in International Law* (Cambridge University Press 2005).; Jan Paulsson, 'Enclaves of Justice', *The Rule of Law Conference*, University of Richmond, 12 April 2007, < [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1707504](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1707504)>, accessed on 15 October 2013. For a counter argument, see David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge University Press 2008).

<sup>345</sup> In the same vein, Verhoosel has highlighted two ways in which WTO can come into play in investment arbitrations in the context of the interpretation of fair and equitable treatment. Firstly is by way of A38 of the ICJ Statute as applicable law and the second one is by way of Article 31(3)(c) of the VCLT as interpretative context. This thesis is in line with the second method which requires further assessment of the wider context of general international law. See Verhoosel, 'The Use of

prohibiting national –based discrimination measures and regards protectionism as a red flag that indicates the breach of the provision. In both jurisprudences, the existence of protectionist measures can be indicative of an irrational measure unless it can be proven otherwise as a reasonable and legitimate measure under investment arbitrations or fall under the exceptions of GATT Article XX.

### 3.0 The Basis of Comparison

It was not until the emergence of NAFTA Chapter 11 national treatment cases that attention to cross read international investment law version of national treatment with GATT/ WTO occurred.<sup>346</sup> Presuming similarity from the long tradition of national treatment in GATT/WTO, some investment tribunals have considered the relevance of the jurisprudence in the interpretation of national treatment.<sup>347</sup>

Although reference to GATT/WTO is already a practice, the basis of doing so has not been properly laid. The tribunals have not examined thoroughly the relevance of GATT/WTO in the context philosophies of national treatment. An examination of national treatment in GATT must not automatically render similar interpretation in

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Investor–State Arbitration under Bilateral Investment Treaties to Seek Relief for Breaches of WTO Law’ (n 121).

<sup>346</sup> The national treatment provision appears in all the basic WTO texts, namely General Agreement on Tariffs and Trade (GATT), General Agreement on Trade in Services (GATS) and Trade-Related Aspects of Intellectual Property Rights (TRIPS). Of the three, GATT contains the most articulated adjudication of national treatment. Cases which have debated the relevance of the GATT jurisprudence are for instance *S.D. Myers Inc. v Government of Canada* UNCITRAL/NAFTA, Partial Award, 13 November 2000; *Pope & Talbot Inc v The Government of Canada* UNCITRAL/NAFTA, Award on the Merits of Phase 2, 10 April 2001; *Methanex Corporation and United States of America* UNCITRAL/NAFTA, Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005; *CPI Inc. v Mexico*, (n 98).

<sup>347</sup> *CPI Inc. v Mexico*, (n 98), para 122; Todd Weiler, ‘NAFTA Investment Arbitration and the Growth of International Economic Law’ [2002] B.L.I 159 <<http://www.dundee.ac.uk/cepmlp/journal/html/vol12/article12-4.pdf>>, accessed on 14 October 2013. In contrast to that, see *Methanex v USA*, (n 19), para 6.

international investment.<sup>348</sup> There is a need of careful examination on the basis of comparison and the relevant principles suitable for transposition. We have seen that the underlying philosophies are similar in the sense that both promote level playing field and competition. Both protect the comparators against discrimination based on nationality. This is a useful parameter of likeness that should be emphasised in a national treatment comparison enquiry in both jurisprudences.

So much on the philosophy, this section then proceeds by looking at the practical interaction between the regimes. To begin with, both GATT/WTO and international investment are part of the bigger branch of international economic law. They are the two main forces that integrate national economy into the international economy which contributes to economic globalisation.<sup>349</sup> The inter-relatedness between trade and investment can also be seen from the initial suggestion to include investment in the Uruguay Round 1994.<sup>350</sup> Investment however remained outside the system due to the non-readiness of states concluding an international investment treaty on a multilateral basis. It became a regime of its own when states began concluding BITs.<sup>351</sup>

Apart from market liberalisation and protection of investment, the two jurisprudences serve similar economic purpose which includes raising the standards of living and greater economic cooperation.<sup>352</sup> Trade and investment treaties contain

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<sup>348</sup> 'Like product' in GATT does not necessarily bring the same interpretation of 'like circumstances' in international investment. See *CPI, Inc. v Mexico*, (n 98), para 121.

<sup>349</sup> Jagdish Bhagwati, *In Defense of Globalization* (OUP USA 2004) 3.

<sup>350</sup> Thomas L. Brewer and Stephen Young, *The Multilateral Investment System and Multinational Enterprises* (New Ed, OUP Oxford 2000) 46.

<sup>351</sup> Alvarez, 'The Emerging Foreign Direct Investment Regime', (n 155) 96.

<sup>352</sup> See preamble to GATT which mentions 'with a view to raising standards of living'. Similar emphasis is in BITs, for instance the US BIT Model 2004 which desires 'to promote greater economic

guarantees and protections, including the national treatment obligation to achieve harmonious trading and investment atmosphere and to avoid states seeking self-interest economic policies.<sup>353</sup>

The resemblance in which both regimes serve is apparent. Both regimes seek at providing a guideline in which foreign investors and imported goods can be subject to domestic regulations. By some scholars, it is regarded as ‘disciplining’ the host and importing states from imposing regulations which are unjustifiable and discriminatory which are against the commitments entered into in WTO and investment agreements.<sup>354</sup>

It is observed that both investments and trade fear the same threat; regulatory barriers in various forms such as taxes, permits and licences which could be discriminatory against foreign trades and investments. In some circumstances, the same government measure can result to claims in both jurisprudences.<sup>355</sup> For instance, Mexico’s imposition of tax on HFCS was challenged in an investment case

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cooperation’ and to ‘maximize effective utilization of economic resources and improve living standards’.

<sup>353</sup> An example of domestic regulation that contributed to trade retaliations was the US-Smoot-Hawley Tariff 1930. See Hudec, ‘Circumventing Democracy’ (n 324); Bussière, Pérez Barreiro, Straub, and Taglioni, ‘Protectionist Responses to the Crisis’ (n 244); Robert E. Baldwin, ‘The Political Economy of Trade Policy’ (1989) 3 *The Journal of Economic Perspectives* 119–135. Similarly, in international investment, discriminatory treatment would cause deprivation of alien property and lead to claims towards the host government which eventually discourage investments.

<sup>354</sup> Walde, ‘Comments on the Discipline of ‘National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3); Kurtz, ‘Balancing Investor Protection and Regulatory Freedom in Investor-State Arbitration: The Complex Search for State Purpose in a National Treatment Inquiry’ (n 267).

<sup>355</sup> *Archer Daniels Midland Co and Tate & Lyle Ingredients Americas Inc v the United Mexican States* ICSID Case No. ARB (AF)/04/05 (NAFTA), Award, 21 November 2007; *CPI Inc. v Mexico*, (n 98). See also Tania S. Voon and Andrew D. Mitchell, ‘Time to Quit? Assessing International Investment Claims Against Plain Tobacco Packaging in Australia’ (2011) 14 *Journal of International Economic Law*, Melbourne Legal Studies Research Paper No. 560, for possible trade and investment claims against plain tobacco packaging. See also Verhoosel, ‘The Use of Investor–State Arbitration under Bilateral Investment Treaties to Seek Relief for Breaches of WTO Law’ (n 121).



*CPI, Inc. v Mexico*<sup>356</sup> and GATT case *Mexico-Tax Measures on 'Soft Drinks' and Other Beverages*.<sup>357</sup> The high probability of the same measure being challenged in both jurisprudences could occur especially in trade-oriented FDIs, when host states introduce non tariff-barriers with local content requirements or other performance requirements.

From the viewpoint of the host states, the national treatment provision in both WTO and investment treaties has caused limited space of regulation.<sup>358</sup> The rapid flow of foreign goods, services and investments creates threat on the host states, especially its concern to determine its own economy. Naturally, host states need to protect their strategic industries and sensitive national security goals relating to matters such as food, communication, transportation, nation building and environment. This common need of regulation and justifications thereof are often the same arguments put forth by host states when confronted with claims of national treatment. There is similarity in the economic logic<sup>359</sup> that has led to presumption of consistency<sup>360</sup> due to the closeness of the subject and the players of the jurisprudences.

The comparison of GATT/WTO and investment in the context of national treatment may appear to some as academic and philosophical as leading to no end or difficult to grasp, but be that as it may, it is undoubtedly a living and practical concern. Apart

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<sup>356</sup>*CPI, Inc. v Mexico*, (n 98), para 47.

<sup>357</sup> Appellate Body Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/AB/R, adopted 24 March 2006, DSR 2006:I, 3.

<sup>358</sup>Henrik Horn and Petros C.Mavroidis, 'Still Hazy after All These Years: The Interpretation of National Treatment in the GATT/WTO Case-Law on Tax Discrimination' (n 122) 40.

<sup>359</sup>Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

<sup>360</sup>There is a presumption of consistency in common principles that also exist in other jurisprudences, even though the context or text differ in each BIT. For instance, the national treatment and MFN provisions which also exist in WTO. See José E. Alvarez, 'The Emerging Foreign Direct Investment Regime' (n 155) 94, 96.

from the closeness of the substantive area of trade and investment, this interaction will remain so as the players in the trade and investment legal fraternity are increasingly merging and linking. This includes the composition of counsels, arbitrators and even academic scholars in both areas. The reflection of this interaction is obvious in investment cases where trade references are deliberated by the tribunals.

Experienced and the structured judicial system of WTO also allows for a more coherent adoption of approaches taken by the panels.<sup>361</sup> International investment tribunals on the other hand operate at a parallel level, where no tribunal can claim superior over the other. The unique absence of the doctrine of judicial precedence has additionally increased the complicated quest for coherence.

The points forwarded contribute to the basis of comparison between the jurisprudences. The real global economic development today involving intra-firm investments and the increasing promulgation of free trade agreements containing investment chapters heightens the closeness of trade and investments.<sup>362</sup> The best approach for the future of both jurisprudences to exist harmoniously is by positive interaction, and the way suggested in this thesis is by coherent interpretation.

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<sup>361</sup> There is a consistency in interpretation in WTO law and many earlier interpretations on substance and procedures survived in subsequent DSB reports. See Isabelle Van Damme, 'Treaty Interpretation by the WTO Appellate Body' (2010) 21 *European Journal of International Law* 605 -648.

<sup>362</sup> Footer, 'On the Laws of Attraction: Examining the Relationship between Foreign Investment and International Trade' (n 318).

#### 4.0 National treatment in WTO

The national treatment provision also appears in all other basic WTO texts, namely General Agreement on Tariffs and Trade (GATT), General Agreement on Trade in Services (GATS) and Trade-Related Aspects of Intellectual Property Rights (TRIPS).<sup>363</sup> GATT however contains the densest jurisprudence on national treatment as it was introduced much earlier and longer than the other texts, prior and after the establishment of WTO.<sup>364</sup> The national treatment on internal taxation and regulation provision in Article III of GATT reads:

1. The [Members] recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.
2. The products of the territory of any [Member] imported into the territory of any [Member] shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. Moreover, no [Member] shall otherwise apply internal taxes or other internal charges to imported or

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<sup>363</sup>Article XVII GATS. The provision is broad applicable ‘to all measures affecting the supply of services’. See also Article 3 in TRIPS.

<sup>364</sup>GATT was signed in 1947 and it was restated in 1994 together with the introduction of other texts in the Marrakesh Agreement Establishing the World Trade Organization. 33 I.L.M. 1140 (1994).

domestic products in a manner contrary to the principles set forth in paragraph 1.

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4. The products of the territory of any [Member] imported into the territory of any other [Member] shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. The provisions of this paragraph shall not prevent the application of differential internal transportation charges which are based exclusively on the economic operation of the means of transport and not on the nationality of the product.

Cases on discrimination emerged rather early in GATT, and scholarly writings are immense.<sup>365</sup> Early discrimination cases have been brought to the GATT panels on various state measures as inconsistent with the national treatment obligation such as state's assistance paid to the purchasers of local machinery,<sup>366</sup> higher excise tax on imported petroleum, certain chemicals and certain imported substances<sup>367</sup> and facially discriminatory laws relating to patent production.<sup>368</sup> More national treatment

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<sup>365</sup> Among the scholars who contributed to discussions on national treatment are GartenVerhoosel, Robert E. Hudec, Henrik Horn, Jurgen Kurtz, Petros C. Mavroidis, Nicholas Di Mascio, Robert Howse, Donald Regan, Michael Ming Du, Alan O. Sykes, Joost Pauwelyn, Federico Ortino, Sungjoon Cho and Mark Liang.

<sup>366</sup> GATT Panel Report, *Italian Discrimination Against Imported Agricultural Machinery*, L/833, adopted 23 October 1958, BISD 7S/60.

<sup>367</sup> GATT Panel Report, *United States – Taxes on Petroleum and Certain Imported Substances*, L/6175, adopted 17 June 1987, BISD 34S/136.

<sup>368</sup> GATT Panel Report, *United States Section 337 of the Tariff Act of 1930*, L/6439, adopted 7 November 1989, BISD 36S/345.

cases were brought under the WTO, some landmark cases are such as the 1992 Malt Beverages Case,<sup>369</sup> Japan-Alcoholic Beverages Case<sup>370</sup> and EC-Asbestos.<sup>371</sup>

In order to establish a national treatment violation for internal taxation, it requires the examination of whether the imported products are like products and whether they are taxed in excess of the domestic products.<sup>372</sup> It is also required by informed application that internal taxation must not be applied so as to afford protection to domestic production.<sup>373</sup> Further, in Note Ad Article III for internal taxation, it requires addressing the question whether the imported and domestic products are directly competitive or substitutable. The articulation of the questions above has already passed a span of more than half a century. In the determination of likeness for instance, it is commented that there is no other place elsewhere which is more enthusiastic than in trade.<sup>374</sup> The experience and the structured judicial system of WTO also allows for a more coherent adoption of approaches taken by the panels.<sup>375</sup>

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<sup>369</sup> The panel interpreted likeness according to the purpose of the measure and the effects thereof, based on the 'so as to afford protection' phrase in Article III(1). The aims and effect test was applied again in US Taxes on Automobiles 1994.

<sup>370</sup> This case marks the rejection of the aims and effects test. However, Hudec opined that the rejection was not absolute and there is still some use in the aims and effect test. E. Hudec, 'GATT/WTO Constraints on National Regulation: Requiem for an "Aim and Effects" Test' (n 123).

<sup>371</sup> This case highlights the application of the competitiveness test.

<sup>372</sup> Article III (2) GATT 1994.

<sup>373</sup> The phrase 'so as to afford protection' is contained in Article III (1) GATT 1994. See also Appellate Body Report, Japan-Alcoholic Beverages II, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:I, p 27-31.

<sup>374</sup> Joost Pauwelyn used the phrase 'obsession with likeness' and suggested to focus on the impermissible criterion that is discrimination based on national origin. However, it is submitted in this thesis that examination of likeness is equally necessary and unavoidable especially in cases of de facto discrimination and in order to determine the covered trade or investments. See Joost Pauwelyn, 'Comment: The Unbearable Lightness of Likeness' in Marion Panizzon, Nicole Pohl and Pierre Sauvé (eds), *GATS and the Regulation of International Trade in Services* (Cambridge University Press 2008).

<sup>375</sup> The shift or mixture of approaches taken i.e the traditional physical characteristic test, the aims and effects test and competitiveness test is part of the development of the regime yet retaining a considerable degree of consistency. According to V. Damme, there is a consistency in interpretation in WTO law and many earlier interpretations on substance and procedures survived in subsequent DSB reports. See Van Damme, 'Treaty Interpretation by the WTO Appellate Body' (n 361). International investment tribunals on the other hand operate at a parallel level, where no tribunal can claim superior over the other. The unique absence of the doctrine of judicial precedence has

There are also discussions to facilitate trade by including regulations on investments relating to trade in the WTO. The areas of work on trade and investment in WTO can be seen from the Working Group on the Relation between Trade and Investment, the TRIMS and GATS. While GATT concerns products, GATS covers services which contain even closer resemblance in the subject of comparison. Services have no physical characteristics and the transactions are intangible like most investments.<sup>376</sup> They are not concerned at protecting the tariffs or border measures but are subject to the various domestic measures and regulations. Services may also overlap with foreign investment, especially in the third mode of service covered by GATS which requires ‘commercial presence’ where ‘the foreign supplier establishes and controls an affiliate, subsidiary or representative office within the territory of the importing member’.<sup>377</sup> However, the scope of application of GATS is small; only in the service sectors explicitly committed by the members.<sup>378</sup> Being also relatively new, there are a limited number of cases involving GATS violations.<sup>379</sup> The GATS jurisprudence is still uncertain and in need of coherence.<sup>380</sup> It is even said that it is GATS that should

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additionally increased the complicated quest for coherence.

<sup>376</sup>The scope of GATS and the abstract characteristics of services was explained by Zacharias. Zacharias, ‘Article 1 GATS Scope and Definition’ in Rüdiger Wolfrum and Peter-Tobias Stoll (eds), *WTO-trade in services* (BRILL 2008) 40; Nicolas F Diebold, *Non-Discrimination in International Trade in Services: ‘Likeness’ in WTO/GATS* (Cambridge University Press 2010) 4. See also Footer, ‘On the Laws of Attraction: Examining the Relationship between Foreign Investment and International Trade’ (n 318).

<sup>377</sup>Diebold, *Non-Discrimination in International Trade in Services* (n 376) 26; Martin Molinuevo, ‘Can Foreign Investors in Services Benefit From WTO Dispute Settlement? Legal Standing and Remedies in WTO and International Arbitration’ in Marion Panizzon and others (eds), *GATS and the Regulation of International Trade in Services: World Trade Forum* (1st edn, Cambridge University Press 2008) 309.

<sup>378</sup> Note by the Secretariat, Services Sectoral Classification List, MTN.GNS/W/120, dated 10 July 1991. Within the sectors, services are exposed to regulatory measures from every angle of its operation which may overlap with national treatment under investments treaties. See Werner Zdouc, ‘WTO Dispute Settlement Practice Relating to the GATS’ (1999) 2 *Journal of International Economic Law* 295.

<sup>379</sup> Among the cases are Appellate Body Report, *Canada-Autos*, *EC-Bananas III*, *Mexico Telecoms*, *US-Gambling*, *China-Publications and Audiovisual Products*.

<sup>380</sup>Diebold, *Non-Discrimination in International Trade in Services* (n 376) 5.

learn lessons from the international investment law, in particular NAFTA, and not the other way around.

In relation to goods, the Trade-Related Investment Measures (TRIMS) was introduced to enhance further the scope of GATT to prohibit investment measures which have impact on trade.<sup>381</sup> The attention to investments issues relating to trade and the introduction of TRIMS rooted from the *GATT Panel Report, Canada — Administration of the Foreign Investment Review Act (FIRA)* case<sup>382</sup> where the United States argued that the FIRA contained trade distorting effects. Although there were doubts as to the competence of panel to hear the issue of investment, it was decided that that the panel could do so as long as within trade-specific issues within the scope of GATT. Thus it concluded that if a government's measure on investment (here the FIRA) could impact or discriminate imported goods, it is inconsistent with Article III:4.<sup>383</sup> GATT still had its limit, not wide enough to cover other aspects of investments covering exports performance requirements.<sup>384</sup> In Article 2 of TRIMs, it prohibits the introduction of trade investment measures that are inconsistent with the obligation of national treatment and general elimination of quantitative restrictions provided for in Article III and XI of the GATT. Trade may be affected if the host states impose measures to reduce imports by foreign investors or promote exports from host states by way of export performance requirements, trade balancing

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<sup>381</sup> Regulation of TRIMs was advanced particularly by developed states during the Uruguay Rounds and was opposed by developing countries that tried to hold on to their existing positions. See Croome, *Reshaping the World Trading System* 256–261.

<sup>382</sup> GATT Panel Report, Canada — Administration of the Foreign Investment Review Act (“FIRA”), L/5504, adopted 7 February 1984, BISD 30S/140.

<sup>383</sup> See at para 6.1.

<sup>384</sup> Patrick F. J. Macrory, Arthur Edmond Appleton, and Michael G. Plummer, *The World Trade Organization: Legal, Economic and Political Analysis* (Springer 2005) 445. See also A. Claire Cutler and Mark W. Zacher, *Canadian Foreign Policy and International Economic Regimes* (UBC Press 1992) 123.

requirements or local content requirements.<sup>385</sup> Although TRIMs have some overlapping aspects with investment, the area is only scoped to investments which give impact on trade. Similar to GATS, TRIMs is relatively new and there have been not many cases decided to shape a matured jurisprudence on national treatment.

## **5.0 ‘Likeness’ in GATT/WTO and International Investment Law Compared**

In both jurisprudences, the national treatment only prohibits discrimination between covered products and investment which are alike. Covered products in trade are ‘like products’, while in investment it is termed ‘like circumstances’ and generally referred to as the ‘comparator’.<sup>386</sup> The complexity of determining likeness is acknowledged in both jurisprudences. In trade, the relativity of the interpretation was described as an ‘accordion’ because it stretches and squeezes in different places where it is applied.<sup>387</sup> Although it is inevitable to determine likeness on a case by case basis, the GATT/WTO panels generally applied the basic approach set in the 1970 Report of the Working Party on Boarder Tax Adjustments which are the product’s end uses in a given market, consumers’ tastes and habits, which change from country to country and the product’s properties, nature and quality.<sup>388</sup> The likeness test did not stop at examining the physical characteristics of the products, but to the processes involved in production, the competitive nature of the products and the likeness of the products from the regulatory point of view.

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<sup>385</sup> Examples of inconsistency is also illustrated in the Annex of the TRIMs Agreement. See also ‘Elimination of TRIMs: The Experience of Selected Developing Countries’ (United Nations Conference on Trade and Development 2007) 2.

<sup>386</sup> Vandevelde, *Bilateral Investment Treaties* (n 2) 338.

<sup>387</sup> Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:I, 97, p 21.

<sup>388</sup> Report of the Working Party on Boarder Tax Adjustments, BISD 18S/97, para 18.



The relevance of GATT/WTO to investment in the context of national treatment has become a much debated subject. There is no consensus of whether GATT/WTO is relevant or irrelevant to investment. In *Methanex v USA* for instance the GATT/WTO is a non-comparable regime and its relevance was rejected in totality. On the other hand in other cases such as *CPI Inc. v Mexico* and *SD Myers*, the GATT/WTO approach is more welcomed.<sup>389</sup> There is always a tendency that GATT/WTO is referred to despite the contextual differences that may exist<sup>390</sup> due to the long tradition of national treatment in international economic practice.<sup>391</sup> Kurtz highlighted this phenomenon in the investment arbitral practice before reaching individual juridical approaches.<sup>392</sup>

The subsequent part of this chapter scopes itself to study the most articulated interpretation tools available in GATT/WTO in determining likeness. The tests are the traditional physical characteristic approach, the aims and effects test, the directly competitive or substitutable approach (DCS) the product process doctrine.

### *5.1 Traditional Physical Characteristic Test*

The traditional characteristic test has so far been used in trade cases to examine ‘like domestic products’ as required in AIII:2 GATT. It involves examination of product’s

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<sup>389</sup>For instance, in the case of *CPI, Inc. v Mexico* (n 98) the tribunal considered likeness of the products between HFCS and sugar cane as decided in WTO as ‘highly relevant’ and in the case of *SD Myers*, the tribunal acknowledged GATT/WTO’s approach in searching for the context of national treatment and applied the same method.

<sup>390</sup>J. H. H. Weiler, ‘Cain and Abel- Convergence and Divergence in International Trade Law’ (n 99)1.

<sup>391</sup>Todd Weiler, ‘NAFTA Investment Arbitration and the Growth of International Economic Law’ [2002] B.L.I., 159.

<sup>392</sup>Jurgen Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’, (n 102) 244.

properties, nature and quality, its end uses (consumers' tastes and habits) and product's classification in tariff nomenclatures.<sup>393</sup> While it is a plausible significant approach in GATT/WTO,<sup>394</sup> it is hard to assume direct adoption of similar exercise in international investment law bearing in mind that the subject of comparison in international investment law are investments which may have no physical characteristics to turn into. Investments vary in their activities, sizes, technologies, forms and orientations.<sup>395</sup>

Investment cases however did turn to this criterion, albeit indirectly. In *Methanex v USA*, the claimant urged for concluding likeness between ethanol and methanol producers due to the competitive relationship between them, and in reference to GATT jurisprudence. The claimant has also indicated that they both produce the same product-oxygenates used in manufacturing reformulated gasoline, suggesting a characteristic approach.<sup>396</sup> This was counterclaimed by the respondent claiming that even if GATT jurisprudence can be compared with, both ethanol and methanol will not satisfy the four part test in the *Asbestos* case as they differ chemically and have different end-users.<sup>397</sup>

The tribunal was in principle obvious in avoiding the direct application or reference to GATT/WTO jurisprudence. However, realising it or not, it had in fact resorted to

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<sup>393</sup> 1970 Working Party Report on Border Tax Adjustments, L/3464, adopted on 2 Dec 1970, BISD 18S/97, para 18. See also Panel Report, *Japan – Taxes on Alcoholic Beverages*, WT/DS8/R, WT/DS10/R, WT/DS11/R, adopted 1 November 1996, as modified by Appellate Body Report WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, DSR 1996:I, 125 para 5.6.

<sup>394</sup> GATT as a commercial agreement, would eventually examine the performance of products in comparison in a given market whether competitive or not, or how any government measure would commercially affect the products. This is very much linked to product's properties, nature and quality, its end uses (consumers' tastes and habits).

<sup>395</sup> The types of investments includes services, licenses, commissions and other investment activities enlisted in investment treaties which may not involve products.

<sup>396</sup> *Methanex v USA*, (n 19), para 23.

<sup>397</sup> *Ibid.*, paras 24-25.

comparison of the characteristics of the products by allowing the more identical comparator to be in the most like circumstances. This is akin to the traditional characteristics test in GATT/WTO.<sup>398</sup> The tribunal in *Methanex v USA* has however adopted too narrow an approach.

The assertion to refer to GATT/WTO by the claimant has some logic which follows through.<sup>399</sup> Comparison of the products of investments assumes likeness in the activities and sectors of the investments. The area of trade and investments are inter-related that it is impossible to strike clear demarcating lines. The approach taken in GATT/WTO is neutral and could also be inherent in investments out of an ordinary examination of likeness. The traditional characteristics test in the GATT/TWO is not mandated by the treaty but was a suggestion by the 1970 Working Party Report on Border Tax Adjustments which was eventually applied in cases. The comparison of the core products of investments at issue could be helpful in understanding the nature and operation of the investment. It is in line with investment protection in such that it is reasonable to look at the investments in the viewpoint of commercial similarity. A notable example of a case that disregarded the examination of investment activity is *OEPC v Ecuador*. In this case, the tribunal made equal petroleum based investment to flowers and agricultural investment which resulted to a broad, cross sector effect of national treatment coverage.

The extent of such approach however, as compared to GATT, is limited. This must not be a conclusive criterion of likeness in investment law but rather its first

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<sup>398</sup> *Ibid.*, para 19.

<sup>399</sup> The tribunal rejected the reference to GATT/WTO and regarded it and international investment as two distinct regimes; See *Ibid.*, para 35.

indicator. Other tests of likeness should take place afterwards.<sup>400</sup> The reason for such a reservation is that too much scrutiny on the physical being of the investment products or services would lead to the loss of contextual implementation of national treatment.<sup>401</sup> The further detail a distinction is made, the more it actually emphasises the similarity.<sup>402</sup> It will also be undesirable to conclude that the examination of likeness is almost close to 'identical' that would undermine the application of the national treatment obligation, being one of the most important cornerstone in international investment treaties.<sup>403</sup> This observation was equally made in the GATT/WTO jurisprudence by Hudec. He claimed that this test sometimes had no purpose oriented criteria and suggested 'competition' as the desired contextual reading of GATT/WTO as opposed to mere examination of physical characteristics.<sup>404</sup>

Caution must also be made if reference is made to tariff related distinctions in WTO as a method to determine physical likeness.<sup>405</sup> Tariffs are deliberately made with fine distinctions so as to allow discrimination to non-participating countries from

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<sup>400</sup>In *Pope & Talbot Inc v Canada*, (n 20), para 78; the tribunal asserted that as a first step to the analysis of likeness, comparison must be made among investments in the same business or economic sector. This approach was also adopted in *Parkerings v Lithuania* in determining likeness in most favoured nation claim. See *Parkerings v Lithuania*, (n 257), para 371.

<sup>401</sup>Quality, resemblance, product processes may deviate one from the competitive relationship. See Robert E. Hudec, 'GATT/WTO Constraints on National Regulation: Requiem for an 'Aim and Effects' Test' (n 123) 623; Robert E. Hudec, "'Like Product': The Differences in Meaning in GATT Articles I and III', (n 123).

<sup>402</sup>*UPS v Canada*, Separate Statement of Dean Ronald A. Cass (n 206).

<sup>403</sup>*UPS v Canada*, (n 21), p. 53, *Methanex v USA*, para 19; *ADM v Mexico*, para 202.

<sup>404</sup>E. Hudec, 'Like Product': The Differences in Meaning in GATT Articles I and III' (n 123); E. Hudec, 'GATT/WTO Constraints on National Regulation: Requiem for an 'Aim and Effects' Test' (n 123).

<sup>405</sup>Example of panel reports which adopted tariff classification in determining likeness are *EEC - Measures on Animal Feed Proteins*, BISD 25S/49; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83; *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/9, adopted on 20 May 1996.

benefitting the tariff.<sup>406</sup> Tariff distinctions do not depend on competitive significance, but to limit concessions to products that would not threaten domestic producers. If this is so applied in investment, local industries will always be protected by fine distinctions.

One may also shed light on the recent cases brought by Apple against Samsung in the legal battle over smartphone technologies. It is difficult to determine what is 'like' in very closely similar products. A detailed characteristic test may result to unlikeness, but a broader commercial overview would take into account the competitive relationship between them.<sup>407</sup> This is an example of a case that may be brought under the auspices of both GATT/WTO and investment laws where the question of likeness will be an issue in determining like circumstances or like products. Thus, the traditional characteristics test is helpful to determine likeness in international investment law. However as discussed above, it is limited to assist the determination of economic sector and as a preliminary step before other rigorous assessment of likeness takes place.

## *5.2 Relevance of Competitiveness Test*

In GATT/WTO, a violation of national treatment will likely occur if a measure discriminately detriments the competitiveness of a foreign product as compared to

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<sup>406</sup>Hudec suggested that like products should not allow fine distinctions is involving internal measures. See E. Hudec, "Like Product": The Differences in Meaning in GATT Articles I and III' (n 123).

<sup>407</sup> This case was brought under intellectual property law. The US Court of Appeal granted an Apple an injunction against Samsung. See *Apple, Inc. v Samsung Electronics Co. Ltd., Samsung Electronics America, Inc. and Samsung Telecommunications America, LLC.*, Case No. 11-CV-1846, US Court of Appeals for the Federal Circuit, 14 May 2012. See opposite decision in the UK High Court that rejected the similarity between Apple and Samsung contested products, at *Samsung Electronics (UK) Ltd v Apple Inc* [2012] EWHC 1882 (Pat) (9 July 2012).

local like products. In practice, competition is applied more than the characteristic features and tariff classification.<sup>408</sup> It is examined from the customers' perspective which includes the common end-users,<sup>409</sup> elasticity of substitution (where the consumers consider as alternative or directly competitive and substitutable),<sup>410</sup> and the market place.<sup>411</sup>

The question to be determined is whether competition is a relevant factor in determining likeness in the investment context. Competition as a criterion is not mentioned expressly in international investment treaties.<sup>412</sup> The test was rejected in *Methanex v USA*.<sup>413</sup> Similarly, it was not considered in *UPS v Canada*. The *UPS v Canada* decision however contained a separate statement which criticised this approach. It emphasised that the most natural reading of NAFTA Article 1102 is to give substantial weight to a showing of competitiveness between the investments.<sup>414</sup> The case of *CPI Inc. v Mexico* is perhaps a clearer example of an investment case that acknowledges competition as a factor. The tribunal observed that the tax measure has altered the terms of competition between the investments which were in direct competition.<sup>415</sup>

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<sup>408</sup> Diebold, *Non-Discrimination in International Trade in Services* (n 376) 108.

<sup>409</sup> Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, (n 387) p25.

<sup>410</sup> Appellate Body Report, *Korea – Taxes on Alcoholic Beverages*, WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999, DSR 1999:I, 3, para 114. See also Won-Mog Choi, *'Like Products' in International Trade Law: Towards a Consistent GATT/WTO Jurisprudence* (Oxford University Press, USA 2003) 109.

<sup>411</sup> Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243, para 99.

<sup>412</sup> See Annex 1, Ad Article III GATT.

<sup>413</sup> Article 1102 must be read 'on its own terms and not as if the words "any like, directly competitive or substitutable goods" appeared in it'. *Methanex v USA*, (n 19) para 37.

<sup>414</sup> *UPS v Canada*, Separate Statement (n 206).

<sup>415</sup> *CPI, Inc. v Mexico*, (n 98) para 120.

This thesis asserts that the competition test is the biggest lesson that investment tribunals could learn from GATT/WTO. Similar to GATT/WTO, the underlying economic philosophy of the investment regime is to ensure the economic level playing field in competing circumstances. This is supported by the statements often included in the preambles of many investment treaties to promote competitive equality, economic cooperation or efficiency.<sup>416</sup> This renders a legal basis for the application of the competition test as it guides the national treatment interpretation towards the objects and purpose of the treaties. It is also more significant than mere characteristics test as the latter could misdirect tribunals to simple dismissal or breach in unguided application. Eventually, the competition test brings the examination of likeness closer to the economic context of investment treaties.

The consideration of competitiveness of investment in likeness also corresponds with the general aim of investment treaties to protect foreign investors who have a relatively weaker legal status as compared to local investors. The locals, who possess voting powers, are influential in the determining of favourable treatments, law or legislations either through democratic means or populist preference or manifestos by the government to keep it in power. The introduction of investment barriers through legislative and regulatory measures such as public procurements, incentives and subsidies are particularly obvious in developing countries.<sup>417</sup> The situation of

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<sup>416</sup> The Singapore-China BIT (1985) mentioned 'economic cooperation'. See Singapore-China BIT (1985) < [http://unctad.org/sections/dite/ia/docs/bits/china\\_singapor.pdf](http://unctad.org/sections/dite/ia/docs/bits/china_singapor.pdf)>, accessed on 31 August 2013. NAFTA also provides 'economic cooperation' and to 'enhance competitiveness' of their firms. In Article 102, among the objectives of NAFTA is to 'promote conditions of fair competition'. See NAFTA, < <http://www.worldtradelaw.net/fta/agreements/nafta.pdf>>, accessed on 31 August 2013.

<sup>417</sup> World Development Report 2005, *A Better Investment Climate for Everyone* (n 7).

foreign investors in this aspect needs the rule of law to preserve the non-discriminatory principle.<sup>418</sup>

The argument of construing likeness towards competition is forwarded by Kurtz in his articles.<sup>419</sup> He also notes the natural role that the national treatment provision should play in combatting protectionism by eliminating discriminatory measures detrimental to the competitiveness between foreign and local investments.<sup>420</sup> This thesis expands this discussion by highlighting the intrinsic features of investments that would require attention.

There are a few considerations of competition in the investment context. Firstly, the more appropriate approach to pursue competitiveness is from the ‘viewpoint of the industry’ as compared to consumers in GATT/WTO.<sup>421</sup> Some investments may not have direct consumers as in trade. Competition is thus not necessarily felt from consumerism but from other aspects of investments which are assessable by the industry. Secondly, it is the subject matter of competition or what competition actually strives for. In trade, the competition aim is the market, while in investment it is the investment viability and profit which may not be relatively reducing other investments as a result of one investment’s better treatment. Thirdly, the equality of competitive opportunities<sup>422</sup> strived by investments are not confined to the profit or

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<sup>418</sup> Paulsson, *Denial of Justice in International Law* (n 344); Paulsson, ‘Enclaves of Justice’ (n 344).

<sup>419</sup> Kurtz, ‘The Use and Abuse of WTO Law in Investor-State Arbitration’ (n 40); Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’ (n 102).

<sup>420</sup> Kurtz, ‘Balancing Investor Protection and Regulatory Freedom in Investor-State Arbitration: The Complex Search for State Purpose in a National Treatment Inquiry’ (n 267).

<sup>421</sup> The term ‘industrial comparability’ was introduced in late Prof. Thomas Walde’s article on national treatment. See Walde, ‘Comments on the Discipline of ‘National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3).

<sup>422</sup> Joost Pauwelyn, ‘Recent Books on Trade and Environment: GATT Phantoms Still Haunt the WTO’ (2004) 15 EJIL 575–592.



loss generated from the products, but includes equal taxes, regulations or procedures from the ‘establishment’ to “management,” “conduct” and “operation” and “expansion” of that investment, and up to the final “sale or other disposition” of the same investment.<sup>423</sup> The scope of competition is wider than in the trade context. Furthermore, having assets and business rooted in a foreign country requires even more predictability in government measures including not less favourable treatment.<sup>424</sup>

It is also pertinent to note that while market-based competition test could be applied in almost all (if not all) comparisons of products in GATT/WTO, it may not be an ideal test for investments in certain circumstances. There are investments which do not compete with each other in the market but could be rendered in ‘like circumstances’. Thus, while it is apparent that the existence of competitive relationship between two investments in the same economic sector is evidence of likeness, competition in this aspect is not a comprehensive criterion that should be imposed on tests of likeness. Investments which are not in market competition but in like circumstances still require similar treatment. There could be instances where two investments which are given a construction project on specified sites are treated differently,<sup>425</sup> or in certain energy market where the market is liberalised not to increase competition but to address shortage of power.

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<sup>423</sup> See *ADF v USA* (n 173).

<sup>424</sup> Investment is subject to a wider range of political risks than trade as it operates within the territory of the host state. See Noah Rubins and Stephan Kinsella, *International Investment, Political Risk and Dispute Resolution: A Practitioner’s Guide* (Oceana TM 2005) 23.

<sup>425</sup> *Parkerings v. Lithuania* (n 257). The appropriate test here is to see whether there is competition in investment opportunities.

In terms of substitutability, the differences between products and investments are obvious. Firstly, investments are not substitutable by nature. Even if it is applied, it is hard to assess it from any or whose perspective. Secondly, as an analogy to other non-discrimination principle which does not involve products such as human rights, the likeness test does not go as far as substitutability. Furthermore, the substitutability test will be difficult, unfair and illogical to be applied in international investment for its narrow effect which would consequently defeat the primary aim of national treatment to protect foreign investments against less favourable treatment.

These cautions addressed do not however negate the importance of competition, but rather enhances the relevance and proper application in the context of investment. It is almost ‘a one rule captures all’ test except for only small exceptions of cases. It is therefore suggested by this thesis (as could be seen in Chapter Six) that competition is a significant indicator of likeness, the effect of which would render the host state a bigger burden of proof to claim otherwise.

### *5.3 Aims and Effects Test*

The aims and effects test involves the examination of the basis of a regulatory measure within the determination of likeness. The origin of this approach in GATT/WTO is laid in Article III:1 which specifies that government measures should not be applied to imported or domestic products ‘so as to afford protection’ to

domestic protection. This test was first applied in *US-Malt Beverages* and the Panel in *US-Taxes on Automobiles*.<sup>426</sup>

There are some issues involved if aims and effect test is to be adopted in investment tribunals. The issues are whether protectionism must be established in every national treatment case and whether it is plausible to determine the legitimacy of the measure within the determination of likeness.

Investment treaties do not literally specify ‘protectionism’ as that of GATT/WTO. Kurtz argues that the absence of ‘so as to afford protection’ does not mean that the national treatment cannot be read under the purview of protectionism. It is the underlying political economy that reveals similar risk as in trade.<sup>427</sup> This is particularly a plausible observation, as the purpose of national treatment is to avoid nationality based discrimination. It aims at avoiding both nationality targeted and nationality affected discriminations. Protectionist measures will provide a red flag to a possible breach of the national treatment provision. It is therefore appropriate to scrutinise whether the measure has protectionist aims and whether it discriminately affects foreign investors. There are at least two positive effects of construing protectionism, firstly is that it will lessen the broad application of discrimination and secondly, it feeds the national treatment principle a purpose, context or direction.

The investment regime could learn from the clear interconnection between protectionist measures and competitive opportunity made by the Appellate Body in *Japan-Alcoholic Beverages*. The Appellate Body mentioned:

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<sup>426</sup> Mireille Cossy, ‘Some Thoughts on the Concept of “Likeness”’ in Marion Panizzon, Nicole Pohl and Pierre Sauvé (eds), *GATS and the Regulation of International Trade in Services* (Cambridge University Press 2008) 342.

<sup>427</sup> Kurtz, ‘Balancing Investor Protection and Regulatory Freedom in Investor-State Arbitration: The Complex Search for State Purpose in a National Treatment Inquiry ’ (n 267) 8.

The broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. More specifically, the purpose of Article III "is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production'". Toward this end, Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products.<sup>428</sup>

The difference is that in the investment context, it is done the other way around. As it is clear that investment treaties are intended to provide protection to foreign investors in the form of equality of competitive conditions by way of national treatment, protectionist aims should be regarded as the adversary and be combatted.

Investment cases have so far put more importance to the second part of the aims and effects test in the assessment of de facto discrimination. The search for protectionist aims has been avoided despite the relevance or assistance that it may cast on the legitimacy of the measure.<sup>429</sup> The aim test in GATT requires a test to examine that discrimination was a 'desired outcome' rather than a 'non-incidental consequence'. Construing protectionist aims is regarded as 'a surmountable burden to the Claimant', much of which revolve around construing the whole matter as one of finding the 'intent' rather than a more objective finding of 'aim'.<sup>430</sup> The Japan-Alcoholic Beverages II has provided a helpful insight on how to construe

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<sup>428</sup> Appellate Body, Japan-Alcoholic Beverages, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996: I, 97, p.16.

<sup>429</sup> *Methanex v USA*, (n 19) para 23. In the case of *CPI Inc. v Mexico*, the claimant persuaded the tribunal to apply aim and effect test, although not worded as so, to look at the protectionist legislation designed (para 55), but the tribunal seemed to examine the effect test regardless whether the tax was to raise Mexican revenue or assist the Mexican sugar industry in time of crisis, the tax would still produce an effect upon the HFCS producers. See *CPI Inc. v Mexico*, (n 98) para 55, 119.

<sup>430</sup> This matter is elaborated in Ch. 6 in the discussion of protectionism and application of the aims and effects test in investment disputes.

protectionist aims. It can be done by ‘objective analysis of the structure and application of the measure in question’ and ‘its protective application’ from the ‘design, the architecture and the revealing structure of the measure’.<sup>431</sup> The challenge of ‘regulatory protectionism’ is recognised in the GATT/WTO jurisprudence. This term emerged to respond to new protectionisms that took place.<sup>432</sup> In the Beef Hormone case for instance, facially non-discrimination policy may also constitute regulatory protectionism.<sup>433</sup>

The aims and effect approach means that the regulation will be the subject of scrutiny. The logic of this can be seen in the GATT/WTO *US-Malt Beverages* case, where the regulatory distinction which marks the characteristics of ‘low’ and ‘high’ alcohol was alleged to be motivated by protectionist aims.<sup>434</sup> Rather than construing the characteristics of the products, the panel construed the underlying reasons of such distinction. As the underlying reason was motivated by protectionist aim, it rendered the characteristic distinction arbitrary. The approach in this case was however not adopted in *Japan-Alcoholic Beverages* (despite its emphasis on protectionism) which preferred to keep the examination of ‘so as to afford protection’ as a separate inquiry. This may be understandable in the trade context where the physical characteristics are obvious and that comparison can be made therefrom, but in the context of investment, the protectionist aim can be embedded in

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<sup>431</sup> *Japan-Alcoholic Beverages II*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, p. 29. See also the conclusion of the Appellate Body in the case of Canada Periodicals on how the magnitude of the differential taxation, the several statements of the Government of Canada’s explicit policy objectives in introducing the measure and the demonstrated actual protective effect of the measure and the design and structure of Part V.1 of the Excise Tax Act was clearly to afford protection to the production of Canadian periodicals. *Canada-Certain Measures Concerning Periodicals*, WT/DS31/AB/R, AB-1997-2, adopted 30 June 1997, page 32.

<sup>432</sup> Sykes, ‘Regulatory Protectionism and the Law of International Trade’ (n 332).

<sup>433</sup> *EC Measures Concerning Meat and Meat Products (Hormones)*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR1998:I, 135.

<sup>434</sup> *US-Malt Beverages Case United States - Measures Affecting Alcoholic and Malt Beverages*, Report of the Panel adopted on 19 June 1992 (DS23/R – 39S/206).

the investments constituting the regulatory differences and would be inevitable to be determined in the likeness enquiry. The examination of the protectionist motivation could be conducted together with the assessment of the reasonableness or rational of the regulatory measure.<sup>435</sup>

Be that as it may, it all boils down to whether the measure is rational or reasonable. The protectionist aim is a significant indicator of a likely irrational measure. In this aspect, international investment treaties are analogous to the trade law as both regimes call for a rational and reasonable basis for the difference of treatment. The GATT/WTO in the *chapeau* of Article XX exception clause prohibits arbitrary or unjustifiable discrimination between countries even where discriminatory regulations are necessary.<sup>436</sup> Although one may argue that the absence of a similar Article XX exception would result to a non-guarantee of the justifications, the investment treaty interpretation is nevertheless subjected to the reasonableness or rational of the measure regardless of any ground. The word ‘rational measure’ appears in many investment cases. Rational relates to the ‘policy objective’ of a measure which could assist the definition of ‘circumstances’ of the investments. It is inherent in international investment law as an international legal instrument. It was also emphasised in the OECD Declaration on International and Multinational Enterprises.

#### *5.4 Relevance of Product Process Doctrine (PPM)*

The product process doctrine (PPM) examines and regulates the processes involved in the production. Such regulation may be discriminatory and exposed to allegations

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<sup>435</sup> This thesis hence suggests that there are circumstances when the assessment of likeness should be merged with the assessment of justification for a meaningful interpretation of national treatment. See Ch.5 and 6 on independent and merged justification methodology.

<sup>436</sup> The *chapeau* constitutes an additional requirement to invoke Article XX apart from the exceptions listed.

of GATT/WTO violation for restricting trade. This is not only a matter of interest to the traders who quest for freer trade, but to the importing country in order to pursue domestic or national interest and the non-governmental agencies especially when involving health, safety or the environment.<sup>437</sup>

In GATT/WTO, there is no direct suggestion that products or investments should be differentiated based on the 'processes' of products. It was however applied in a number of GATT/WTO cases. To mention as examples are the *Tuna/Dolphin* case<sup>438</sup> where the US imposed adoption of dolphin friendly techniques on fishers, and the *Turtles* case<sup>439</sup> where every U.S. trawler fishing waters inhabited by sea-turtles must be equipped with a Turtle Excluder Device (TED).<sup>440</sup> On one side, PPM is said to be an effective tool to promote environment, health and safety standard but on the other, it is also criticised for exposing room for unilateral and extrajurisdictional dictation of domestic standards or societal value<sup>441</sup> which could press developing countries and overexert the scope of interpretation.<sup>442</sup>

While in trade the question is whether two products can be considered unlike because of the 'process', in the investment context the same question can perhaps be asked to test likeness based on the 'operation' or 'investment processes' of the

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<sup>437</sup> 'Climate Change, the Kyoto Protocol, and the World Trade Organization: Challenges and Conflicts' Sustainable Development Law and Policy, Volume 6 Issue 2, 2006.

<sup>438</sup> United States-Restrictions on Imports of Tuna, 30 ILM (1991) 1594; United States-Restrictions on Imports of Tuna, 33 ILM (1994) 936.

<sup>439</sup> Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755.

<sup>440</sup> See also *EC-Certain Measures Prohibiting the Importation and Marketing of Seal Products* (DS369).

<sup>441</sup> Diebold, *Non-Discrimination in International Trade in Services* (n 376) 6.

<sup>442</sup> Robert Howse and Donald Regan, 'The Product/Process Distinction - An Illusory Basis for Disciplining 'Unilateralism' in Trade Policy' (2000) EJIL, Vol. 11 No.2 p249-289 See also Robert Howse, 'The Appellate Body Rulings in the Shrimp/Turtle Case: A New Legal Baseline for the Trade and Environment Debate' (2002) 27 Columbia Journal of Environmental Law 491.

investments. Can an investment be unlike if it operates in a way which could cause damage to the environment or infringe human labour rights or hazardous to health and safety as compared to other investments in the same sector? There is a tendency for tribunals to compare investments from the viewpoint of the regulatory measure which affect the operation or the investment process of the investment. For instance, in *ADF v USA*, the United States imposed local content conditions (*Buy America*) which affected the claimant's steel fabrication work intended to take place in its facility in Canada. Although the tribunal eventually rejected the claim because of the absence of relevant competitive situation, the whole idea of comparison was made on the process or operation of the investment.<sup>443</sup>

It is understandable that in GATT/ WTO the issue of PPM is hotly debated, mainly because the comparison of likeness involved should be on 'like products', an explicit limitation in the national treatment provision. Any comparison other than the physical characteristics of the products (in this sense the non-physical aspects (NPA)), should be discarded.<sup>444</sup> However, the PPM may be a lot useful in international investment considering that the search is on 'like circumstances' of the investments. Although there may be views that by introducing the PPM in investment law, it is as if an attempt to search for the dissimilarities of two investments rather than 'likeness' as manifested in the investment treaties, the two tests actually serves the same end.<sup>445</sup> While the foreign investors need to prove likeness, the host states have to prove unwise. This adverse effect is a natural

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<sup>443</sup> In this case, the rationale of the Buy America condition was not deliberated in depth by the tribunal. See *ADF v USA* (n 173).

<sup>444</sup> Christiane R. Conrad, *Processes and Production Methods (PPMs) in WTO Law* (Cambridge University Press 2011), Cambridge International Trade and Economic Law 151.

<sup>445</sup> For example, two investments processing wood are considered alike from the surface and nature of their investments but by applying PPM, the environmental compliance for instance is scrutinised. This exposes the investments to the likelihood of being unlike.



examination in indicating a matter in law.

The other concern of PPM in GATT/WTO is that it involves imposition of extraterritorial standards to other countries. This has less impact in investment as protected investments are only those operating inside the host state. It appears to be appropriate for host states to take regulatory measure to safeguard its own domestic environmental, health, safety or other legitimate measures within its own territory as long as they are reasonable.<sup>446</sup>

By the application of PPM and aims and effects test, it will give impact on the sequence determination of likeness and its rational. The determination of likeness will occur simultaneously if not after the rational and the effect the measures are determined. This is against the conventional method suggested in investment tribunals, presumably familiarised from GATT/WTO which justifies a measure after a violation has occurred by way of Article XX (*General Exceptions*). Although one may see the absence of similar Article XX in most investment treaties as a deficiency, it actually also open room for a few advantages. Firstly, it allows more flexibility for government regulatory measure to be justified as opposed to the closed subheadings as in Article XX. Secondly, a regulatory measure will not be regarded as breaching the national treatment obligation before the examination its rational and justification.<sup>447</sup> Thirdly, it avoids redundancy and leads to a practical assessment of likeness.

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<sup>446</sup> *Feldman v Mexico*, (n 15) para 170.

<sup>447</sup> Legitimate regulatory measure should be 'redeemed' not justified'. Sungjoon Cho, *Free Markets and Social Regulation: A Reform Agenda of the Global Trading System* (Kluwer Law International 2003) 67.

## 6.0 Legitimate Regulatory Measures

The GATT/WTO introduces a separate assessment of justification after a violation has occurred. This is done by invoking one of the exceptions in Article XX. Article XX of GATT lists exceptions among others; measures which are necessary to protect public morals, to protect human, animal, or plant life or health, secure compliance with laws or regulations which are not inconsistent with GATT, protection of national treasures of artistic, historical value and conservation of exhaustible natural resources.<sup>448</sup> These exceptions constitute non-economic societal values that balance the trade obligations.

A noticeable number of investment agreements are gearing towards this approach either by expressed reference or incorporation of similar exceptions.<sup>449</sup> Some writings have sceptically expressed the role of the general exceptions in international investment law.<sup>450</sup> It could be agreed along this line that the inclusion of the general exceptions would result to a restricted assessment of regulatory measures, especially in response to new issues in the increasingly complex economic world and regulatory states. If this incorporation is intended to balance the non-economic

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<sup>448</sup> Article XX provides other exceptions including those relating to products of prison labour and trade in gold and silver.

<sup>449</sup> See for instance Article 200 (1) of the China-New Zealand FTA which adopts an expressed reference approach, stating that ‘for the purposes of this Agreement, Article XX of GATT 1994 and its interpretative notes and Article XIV of GATS (including its footnotes) are incorporated into and made part of this Agreement, mutatis mutandis.’ < <http://www.chinafta.govt.nz/1-The-agreement/2-Text-of-the-agreement/18-Chapt-17-Exceptions/index.php> > , accessed on 4 September 2013. An example of incorporation of similar list of exception are the ASEAN Comprehensive Investment Agreement (ACIA), the Singapore-Jordan BIT in Article 18 and the Energy Charter Treaty (ECT) in Article 24(2)(b), all available at < <http://cil.nus.edu.sg/rp/pdf/2009%20ASEAN%20Comprehensive%20Investment%20Agreement-pdf.pdf> >; < [http://unctad.org/sections/dite/ia/docs/bits/Singapore\\_Jordan.pdf](http://unctad.org/sections/dite/ia/docs/bits/Singapore_Jordan.pdf) >; < [http://www.encharter.org/fileadmin/user\\_upload/document/EN.pdf](http://www.encharter.org/fileadmin/user_upload/document/EN.pdf) >; accessed on 4 September 2013.

<sup>450</sup> See Céline Lévesque, ‘The Inclusion of GATT Article XX Exceptions in IIAs - A Potentially Risky Policy’ in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013); Legum and Petculescu, ‘GATT Article XX and International Investment Law’ (n 319).

societal values, it is submitted that it could alternatively be done by the application of general principles already available in international law such as the principles of reasonableness and proportionality. Having said that, this thesis however does not go as far as suggesting the incorporation or non-incorporation or of a similar Article XX, but rather focuses on how the interpretation of legitimate regulatory measure generally in the national treatment context could be benefitting investment law.

A valuable lesson that could be learnt is from the *chapeau* of Article XX which requires that measures must not be applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade. While the lists itself constitutes similar assessment of rational and legitimacy of the government measures and reasonable nexus to rational government policies as in investment disputes, the *chapeau* filters the invocation which is akin to the principles of reasonableness and proportionality. The principle of proportionality in particular has an unclear standing in investment arbitrations.<sup>451</sup> In the cases of *US-Gasoline* and *US-Shrimp* for instance, the measures were provisionally justified under Article XX (g) but the application of the measure did not pass the requirements of the *chapeau*.<sup>452</sup> The Appellate Body in *US-Shrimp* described the *chapeau* as ‘the prevention of the exceptions of [Article XX] and ‘one expression of the principle of good faith’.<sup>453</sup> Looking at the *chapeau* in this perspective will support the application of the proportionality test in investment arbitrations.

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<sup>451</sup> The elaboration of the need of proportionality test and its lack of explicit application is in Ch.5.

<sup>452</sup> The Panel in the case of *US-Automotive Spring Assemblies* emphasised that the *chapeau* of Article XX is not on the measure itself, but on the application of the measure. Peter van den Bossche, *The Law and Policy of the World Trade Organization: Text, Cases and Materials* (2nd Ed., Cambridge University Press 2008) 651. See Appellate Body Report- *US-Shrimp*, paras 185-186 and Appellate Body Report-*US-Gasoline*, p28-29; *US-Automotive Spring Assemblies*, GATT B.I.S.D (30th Supp) at 125, para 56 (1983), adopted on May 26, 1983.

<sup>453</sup> Appellate Body- *US-Shrimp*, para 151, 158.

Similarly referring to the importance of proportionality is the use of the term ‘necessity’ in Article XX. Not all the exception list contains this term. This suggests a less stringent requirement in the items.<sup>454</sup> Although the necessity test is somewhat problematic in the GATT/WTO jurisprudence, it could be discerned from the most striking view that it only allows exceptions if there is ‘no alternative measure’.<sup>455</sup> This is also known as the ‘least restrictive measure’ or ‘least GATT-inconsistent measure test’.<sup>456</sup> The Appellate Body in the case of Appellate Body Report, *Korea-Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, (*Korea-Beef AB Report*) mentioned;

‘As used in Article XX(d), the term "necessary" refers, in our view, to a range of degrees of necessity. At one end of this continuum lies "necessary" understood as "indispensable"; at the other end, is "necessary" taken to mean as "making a contribution to." We consider that a "necessary" measure is, in this continuum, located significantly closer to the pole of "indispensable" than to the opposite pole of simply "making a contribution to".’<sup>457</sup>

However the application the necessity test would potentially severely limit the host states’ regulatory space in pursuing the democratic mandate. The relevance of the necessity test itself is debated in the trade context as intruding or causing excessive

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<sup>454</sup> Christopher Doyle, ‘Gimme Shelter: The Necessary Element of GATT Article XX in the Context of the China-Audiovisual Products Case’ (2011) 29 Boston University International Law Journal 143.

<sup>455</sup> If there is ‘no alternative measure consistent with the General Agreement, or less inconsistent with it’. See Thailand-Cigarettes, para 75. See also US-337 of the Tariff Act 1930, GATT B.I.S.D (36<sup>th</sup> Supp) at 345, para 5.26 (1989). As for the uncertain and ambiguous nature of the interpretation of necessity, *Ibid*.

<sup>456</sup> Dukgeun Ahn, ‘Environmental Disputes in the GATT/WTO: Before and after US - Shrimp Case’ (1998) 20 Michigan Journal of International Law 819.

<sup>457</sup> Appellate Body Report, *Korea-Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, 161, WT/DS161,169/AB/R (Dec. 11, 2000), para 161.

infringement on the economic sovereignty of member states.<sup>458</sup> The difference of subject of regulation between trade and investment becomes handy to justify difference at this particular juncture. While the effect of trade is limited to the movement of goods, investment tribunals have to consider the effect of the investments considering the long term presence of the investments themselves on its territory. Hence, in this particular aspect, while the necessity test could cast guidance in the proportionality test, the investment law is not entrenched to prohibit any restrictive measure to the investors but rather unreasonable ones proportionately executed.

There is a point to be commented whether there is such thing as ‘justifiable discrimination’ in investment law. It is argued in scholarly articles that by including exception list, it is as if recognising that international investment law permits justifiable discrimination.<sup>459</sup> It is submitted here that this is more of a superficial issue as firstly, it is a normal legal practice that rules have exceptions and secondly that when there is discrimination there is no harm of calling a discrimination a discrimination, a spade a spade, and then having it justified. This is the approach already adopted in the three prong test in the context of national treatment. As will be explained in Chapter Six, the construction of likeness involves flexibility in which the justification of the measure can be assessed simultaneously or separately. Thus, the examples that one can discern from investment cases such as *Methanex v USA*, would suggest that the measure was discriminatory but justifiable. The point rather is that exceptions exist in the form of justification, deference or legitimacy of the

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<sup>458</sup> Ahn, ‘Environmental Disputes in the GATT/WTO’ (n 456).

<sup>459</sup> Legum and Petculescu, ‘GATT Article XX and International Investment Law’ (n 319); Lévesque, ‘The Inclusion of GATT Article XX Exceptions in IIAs - A Potentially Risky Policy’ (n 450). This thesis agrees however that the inclusion of similar Article XX would not yield significant difference to investment arbitration.

measure with or without the physical exception list and could be conducted flexibly whether in the assessment of likeness or afterwards. Or if one is to put it another way, the GATT/WTO jurisprudence methodology of ‘violation first, exception later’ can occur in investment disputes on national treatment in certain circumstances.

## 7.0 Conclusion

This chapter concludes that GATT/WTO is able to provide guidance in the interpretative context of international economic law. The role of competition in particular is essential in guiding the interpretation of likeness closer to achieving the philosophies of national treatment to provide level playing field in investments. It has also highlighted the role of national treatment as an agent to curb protectionism, a common enemy. As to other methods of interpretation of likeness, in particular the aims and effect test and the product process doctrine, it is observed that they are more relevant to the international investment context as compared to trade. While they may be debated heatedly in trade, they may be more welcomed in investment. Last but not least the *chapeau* in Article XX supports the importance of the principle of proportionality that should be further developed in investment disputes. All in all, the comparative exercise with the GATT/WTO by way of analogy has resulted in positive findings that should be able to assist the evolving principle of national treatment in international investment law.<sup>460</sup>

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<sup>460</sup> Walde, ‘Comments on the Discipline of ’National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3); Roberts, ‘Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System’ (n 322).

## THE RELEVANCE OF THE EU LAW TO THE INTERPRETATION OF NATIONAL TREATMENT

### 1.0 Introduction

The comparison between international investment law and the European Union (EU) law is hoped to convey a fresh discussion in the area. While the current attention between the two jurisprudences is heavily on the new EU competence on investment treaties and its impact on the current bilateral investment treaties (BITs) of the member states, this thesis embarks on a positive dimension.<sup>461</sup> It primarily seeks the possibility of taking lessons from the EU's vast jurisprudence on non-discrimination from two areas of the law, namely free movement of capital (FMoC) in Article 63(1)

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<sup>461</sup> The conflict between the EU law and intra-EU bilateral investment treaties is intense as they contain overlapping or similar subject matters. Due to the same regulatory measures, the ECJ fears that by maintaining BITs they may interfere with the EU law, for instance, when it chooses to restrict capital movements in accordance to Article 65 TFEU (ex Article 58 TEC). The existence of the EU law and intra-EU BITs is described to be from 'independent parallelism' into 'increasing interaction' between the two jurisprudences. See Case C-249/06 *Commission of the European Communities v Kingdom of Sweden* [2009] ECR I-1335 and Case C-205/06 *Commission v Austria* [2009] ECR I-1301. See also Nikos Lavranos, 'Bilateral Investment Treaties (BITs) and EU Law' (2010) <[http://www.esil-en.law.cam.ac.uk/Media/Draft\\_Papers/Agora/Lavranos.pdf](http://www.esil-en.law.cam.ac.uk/Media/Draft_Papers/Agora/Lavranos.pdf)>, accessed on 14 October 2013 ; Angelos Dimopoulos, *EU Foreign Investment Law* (Oxford University Press 2011). So much as this research is not concerned about the intra BITs entered into by member states, it will not examine the conflicts which have arisen or potential to arise therefrom. It proceeds from this interaction only by acknowledging the similarity of regulatory interest between the two. Just as the EU views restriction of capital movement as an impediment to its aim of an internal market, international investments agreements also regards the introductions of taxes amounting to indirect interventions which could give rise to substantive claims under the agreements. For the discussion of taxes and indirect intervention, refer to Thomas W Walde and Abba Kolo, 'Investor-State Disputes: The Interface Between Treaty-based International Investment Protection and Fiscal Sovereignty' (2007) Vol.35 Intertax 424.

TFEU ex Article 56(1) EC and freedom of establishment (FoE) in Article 49 TFEU (ex Article 43 TEC).<sup>462</sup>

The focus on FMoC and FoE is due to the similarity in the obligation of the member states to adhere to the non-discriminatory principle in investment related area. Member states can only exercise their competence in regulation consistently with the European Union law, i.e the four freedoms and the general non-discrimination clause. This affect the member state's regulatory space, in particular matters of direct taxation (income and incorporate taxes) which are preserved to the member states.

The ECJ has many years of experience in dealing with discriminatory measures of the member states. This is evidenced in its body of jurisprudence. It evolved since the formation of the European Economic Community (EEC) in 1957 and by case laws decided by the European Court of Justice.<sup>463</sup>

This chapter mainly deals with the direct taxation cases as they constitute a significant piece of free movement of capital and freedom of establishment cases in the EU jurisprudence.<sup>464</sup> They contribute substantial obstacle to the full

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<sup>462</sup> Treaty of Lisbon (Amending the Treaty on European Union and the Treaty Establishing the European Community), (2007/C 306/01), signed on 13 December 2007, entry into force 1 December 2009, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2007:306:0001:0010:EN:PDF>, accessed on 12 September 2013.

<sup>463</sup> The EEC was established in the Treaties of Rome 1957 and was amended several times. Among the important ones are the Single European Act (1986), Treaty on European Union, known as the "Maastricht Treaty" (1992), Treaty of Amsterdam (1997), Treaty of Nice (2001) and the Treaty of Lisbon (2007). The Treaty of Lisbon marks the current framework of EU law which consists of the Treaty of European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU), the latter containing the Treaties of Rome.

<sup>464</sup> Discrimination claims are brought in many direct taxation cases, which has at least of 20 years of experience after the case of *Avoir Fiscal* in 1986. Tom O'Shea suggested that there was an earlier case, *Humblet v Belgian State* on direct taxation preceding *Avoir Fiscal*. O'Shea, 'Freedom of Establishment Tax Jurisprudence: *Avoir Fiscal* Re-visited' (n 128). See also Case 270/83 *Commission*



establishment of the EU, as observed in the case laws of the two freedoms.<sup>465</sup> The domestic legislations which are not wholly or mainly relating to taxation is not excluded in the tax exemptions in many treaties.<sup>466</sup> As tax is normally not defined in investment treaties, it has created a difficult and blurry area of direct or indirect taxations. At the end, the test is to determine the substance of the discriminatory measure (which may include tax measures) that would enable a claim under national treatment.<sup>467</sup> Furthermore, tax regulations are expected challenges that must be faced by international investment in a foreign territory. This explains the existence of past investment cases that involved challenges of tax measures of the host states, to name a few, taxes on soft drinks (*CPI Inc. v Mexico* and *ADM v Mexico*) and tax rebates in *Feldman v Mexico* and *OEPC v Ecuador*.<sup>468</sup>

Other forms of regulatory measures which impede or discriminate the freedoms will be construed if they are featured within the two freedoms.<sup>469</sup> Landmark cases in which important general principles are derived from, although originated outside FMoC and FoE, such as the ‘rule of reason’ in *Cassis de Dijon* will be acknowledged in the discussions.<sup>470</sup>

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*v France* (‘*Avoir Fiscal Case*’)[1986] ECR 0273; Case 6/60 *Humblet v Belgian State* (‘*Humblet*’) [1960] ECR 559.

<sup>465</sup> Paolo Arginelli, ‘The Discriminatory Taxation of Permanent Establishments by the Host State in the European Union: a Too Much Separate Entity Approach’ (2007) 35 *Intertax* 82–116.

<sup>466</sup> For instance, the Mongolia-Korea BIT in Article 7 has excluded from its national treatment provision ‘any international agreement or domestic legislation relating wholly or mainly to taxation.’ See Korea-Mongolia BIT, signed 28 March 1991, <[http://unctad.org/sections/dite/ia/docs/bits/korea\\_mongolia.pdf](http://unctad.org/sections/dite/ia/docs/bits/korea_mongolia.pdf)>, accessed 24 September 2013.

<sup>467</sup> Walde and Kolo, ‘Investor-State Disputes: The Interface between Treaty-based International Investment Protection and Fiscal Sovereignty’ (n 461).

<sup>468</sup> *ADM v Mexico*, (n 355), para 80; *CPI Inc. v Mexico*, (n 98), para 40; *Feldman v Mexico*, (n 15), para 7, *OEPC v Ecuador*, (n 18), paras 29-32.

<sup>469</sup> However, as the scope of the cases brought under FoE and FMoC are mostly relating the member states’ capital and establishment policies, we could rarely see other variance of justifications of exceptions brought as most are fiscal-based justifications.

<sup>470</sup> *Cassis de Dijon*, (n 35).

This chapter highlights the increasing relevance of the EU law due to the recent development of economically integrated communities involving investment agreements. A striking example is the ASEAN Comprehensive Investment Agreement (ACIA).<sup>471</sup> Other examples are the African Economic Community (AEC) and at a lesser integration level, the CAFTA-DR and NAFTA.<sup>472</sup> The questions are whether the function of non-discrimination principle in these instruments is similar to the EU and if so, whether they can adopt the EU approach in construing non-discrimination cases. This chapter will primarily explore these interesting possibilities and put forth the observations and suggestions on the matter.<sup>473</sup>

Before any transposition or ‘benefiting the tools of interpretation’ is proposed, this chapter begins with an examination of the underlying philosophy of the EU law so as to situate the whole discussion into its proper perspective. This basic process is also essential to lay points of similarity and demarcation which calls for the compatibility of the two jurisprudences at hand. Such piece of material deserves emphasising so as to provide an informed and well-studied analysis.

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<sup>471</sup> ASEAN Comprehensive Investment Agreement (ACIA) 2009, signed on 26 February 2009, <[http://www.thaifita.com/ThaiFTA/Portals/0/acia\\_sign.pdf](http://www.thaifita.com/ThaiFTA/Portals/0/acia_sign.pdf)>, accessed on 12 September 2013.

<sup>472</sup> Treaty Establishing the African Economic Community (AEC), signed 3 June 1991, entered into force May 1994, <[http://www4.worldbank.org/afr/ssatp/Resources/HTML/legal\\_review/Annexes/Annexes%20III/Annex%20III-03.pdf](http://www4.worldbank.org/afr/ssatp/Resources/HTML/legal_review/Annexes/Annexes%20III/Annex%20III-03.pdf)>, accessed 21 September 2013; Central America Free Trade Agreement (CAFTA), signed 28 May 2004, <<http://www.caftalaw.net/cafta-text>>, accessed on 20 July 2013; North American Free Trade Agreement between the Government of Canada, the Government of Mexico and the Government of the United States, 17 December 1992, Can. T.S. 1994 [entered into force 1 January 1994].

<sup>473</sup> This chapter will also shed general observations in respect of other investment treaties with lesser aim of economic integration.

## 2.0 The Underlying Philosophy and the Nature of Integration of the European Union

The EU is a direct effort of peace and prosperity after the World War II in the European region. Geographically, it is located in the areas devastated by war. Demographically in its promulgation, it was entered into by previous warring states. Still bearing the scars of the war, the prevailing view of the time was that economic cooperation would increase cross-border transactions and business settings whilst mitigating tendencies of military conflicts.<sup>474</sup> Thus, there was a determination to avoid possible future conflicts and to curb signs of protectionism which was emerging.<sup>475</sup> The integration of the EU was necessary and urgent in the context of the political economy in the region—inter alia, as it was costly to defend individual states in case of military attacks<sup>476</sup> and that there was a need to rebuild Europe which was physically and economically affected by the war. The six initiating states of the European Community namely France, Germany, Italy, Belgium, Netherlands and Luxemburg embarked in the first cooperation in coal and steel which then led to the promulgation of Treaty of Rome for further integration. The manifestation of achieving economic cooperation is seen in the preambles of the treaties. Article 2 of the Treaty of Rome mentioned:

‘The Community shall have as its task, by establishing a common market and progressively approximating the economic policies of Member States, to

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<sup>474</sup>John R O Neal and Bruce Russett, ‘The Kantian Peace: The Pacific Benefits of Democracy, Interdependence, and International Organizations, 1885-1992’ (1999) 52 World Politics 1; Joseph M Grieco, ‘The International Political Economy Since World War II’ [2001] Columbia International Affairs Online (CIAO) <<http://www.isn.ethz.ch/isn/Digital-Library/Publications/Detail/?lng=en&id=6843>>, accessed on 28 January 2014.

<sup>475</sup>Brita Sundberg-Weitman, *Discrimination on Grounds of Nationality: Free Movement of Workers and Freedom of Establishment Under the EEC Treaty* (North-Holland Pub. Co. 1977) 9.

<sup>476</sup>It was necessary to include the German economy in the integration to avoid conflicts or threats to the neighbouring countries. Europe was very weak after the war to face threat from amongst themselves or the external threat of soviet expansion.

promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increase in stability, an accelerated raising of the standard of living and closer relations between the States belonging to it.’

This is where the EU law takes a step ahead in establishing a higher level of integration and cooperation than what is required in WTO and international investment treaties. The EU has been described as *sui generis* in this sense, as its objective is beyond a mere trade integration. The objective of the common market in the EC Treaty- now ‘internal market’ in the Lisbon Treaty<sup>477</sup> is the distinctive element that requires deeper level of integration and commitment from the member states. This allows the free movement of the production factors which are goods, services, persons and capital (which constitute workers and capital) to enable high mobilisation of the factors of production and to realise the macro-economic objectives as enshrined in the EU.

The integration is supported with institutions of the EU, i.e the EU Parliament, EU Commission, and the ECJ. The EU Parliament ensures the democratic process in the policy making of the EU while the Commission manages the rules and technical harmonisation. The national authorities are obliged to ensure its compliance. At the judicial level, the ECJ interprets and develop the jurisprudence. The relationship between the national law and the EU law is under the principle of supremacy. Whenever there is a conflict between the provisions of EU law and the provisions of

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<sup>477</sup>The Lisbon Treaty embodies the same aim again in Article 2 TFEU.

the domestic (national) law of a member state, then EU law will prevail.<sup>478</sup> The other principles integral to the EU law are the principles of direct effect, proportionality and subsidiarity.

A further analysis of the nature of EU integration would suggest that it is a step towards political integration.<sup>479</sup> The proponents of this idea stem their reasoning from the historical evolution of the EU law. Pescatore regarded political integration as the distant aim of the EU (European Community then) which it tries to achieve after the customs union and economic union. There were drafts in the 1950s to establish a European Political Community and a European Defence Community as a collective effort to curb the advancement of the Soviet Union military but were then aborted. Attempts to create political integration as an aim of the European community is also said to be recorded in the Hague Conference of 1969.<sup>480</sup>

If political integration is found as the dominant philosophy of the EU, the impact on the oneness of the market will be much greater as the power to regulate shifts immensely from the member states to the EU. Because of the constant debates on the extent of the intended political integrations and the exact definition of the European

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<sup>478</sup> Case 26/62, *Van Gend en Loos v Nederlandse Administratie der Belastingen* [1963] ECR1, Case 6/64 *Costa v ENEL* [1964] ECR 585 and Case 11/70 *Internationale Handelsgesellschaft mbH v Einfuhr- und Vorratsstelle für Getreide und Futtermittel* [1970] ECR 1125.

<sup>479</sup> Matej Avbelj, 'Theory of European Union' (2011) 818 *European Law Review* <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1976376](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1976376)> accessed 29 January 2014; Pierre Pescatore (ed), *Law of Integration* (1st edn, Springer 1974) 23.

<sup>480</sup> 'Meetings of the Heads of State or Government' (1970) 1 *E.E.C Bulletin* 12 <[http://aei.pitt.edu/1451/1/hague\\_1969.pdf](http://aei.pitt.edu/1451/1/hague_1969.pdf)>, accessed on 29 January 2014. On the progressive integration of the EU, it is described as an 'irreversible advance' and would continue in the future. See Michael J Geary, 'The Process of European Integration from The Hague to Maastricht, 1969-92: An Irreversible Advance?' [2012] *Debater A Europa* <<http://ftp.infoeuropa.euroid.pt/database/000048001-000049000/000048470.pdf>>, accessed on 29 January 2014.

entity and identity,<sup>481</sup> it is thus important to evaluate the EU law as it is currently representing. For the purpose of this research, it is appreciated that the EU law is a deep ‘economic integration’ which has become the orientation of the ECJ decision makings. First and foremost, the aim of economic integration is apparent and self-explanatory in Article 2 of the TFEU that it shall work for the sustainable development of Europe ‘based on balanced economic growth and price stability, a highly competitive social market economy and aiming at full employment and social progress’. Substantively, it is supported with the freedoms granted which have a profound economic basis, as they are themselves factors of production (goods, services, labour and capital). The establishment of the EU law was heavily grounded on the economic ideas<sup>482</sup> and that the economic philosophy was the ‘aggregate economic phenomena’ which shaped the jurisprudence.<sup>483</sup> In this aspect, the EU historical timeline portrays the shifts towards the betterment of economic integration by the introduction of the Single European Act in 1987, the Maastricht Treaty and the recent Lisbon Treaty with more economic power to the EU. In terms of decisions of the ECJ, it has even been argued that the EU law construes justice in the ‘economistic nature of justice’.<sup>484</sup> It is observed that the ECJ has put the EU agenda in achieving an internal market above national interest, albeit reserving restrictive areas for justifications for member states.<sup>485</sup>

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<sup>481</sup> Terms used relating to the entity and identity of the European Union are generally ‘supranationality’, ‘federalism’ and ‘constitutionalism’.

<sup>482</sup> Philip Allott, *The Health of Nations* (Cambridge University Press 2002) 258 .

<sup>483</sup> *Ibid.*

<sup>484</sup> The tendency of the EU law to construe justice from the economic point of view was criticised as opposed to the ‘perceived notion of justice’. Andrew T Williams, ‘Promoting Justice After Lisbon: Groundwork for a New Philosophy of EU Law’ [2010] *Oxford Journal of Legal Studies*; Andrew T Williams, ‘Taking Values Seriously: Towards a Philosophy of EU Law’ (2009) 29 *Oxford Journal of Legal Studies* 549.

<sup>485</sup> In the case of *Commerzbank*, the court held that the national provision that provides unequal treatment to a German company with a branch in the UK in relation to repayment supplement as compared to UK resident companies is discriminatory and is to the disadvantage of companies having seats in other member states. The fiscal residence justification brought forth by UK was not accepted.

The difference in the nature of integration - the EU being a supra-national entity as opposed to mere 'treaty relationships' of investment treaties- do not necessarily conclude that they are contradictory to each other. The difference generally rests on the degree of integration, but to a considerable extent both jurisprudences strive for economic integration and liberalisation. Both jurisprudences apply the principle of non-discrimination in the same way and are concerned with the same discriminatory measures imposed by the member states/ host states. Where free movement of capital and establishment are granted, they provide a substantial level of investment protection and where investment protection is provided in investment treaties, it provides a substantial level of freedom, vice-versa. The next subsection will explore these similarities.

### **3.0 The Analogy: The EU Law and International Investment Law on National Treatment**

The EU is a regional economic integration which binds its members to achieve an internal market. This is manifested in Article 26(1) and (2) Treaty on the Functioning of the European Union (hereinafter the 'TFEU') (ex Article 14 TEC) which reads:

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Similarly held was in the case of *Halliburton* where the non-resident company set in the EU should be able to enjoy the community freedom of establishment even though it was owned by a US parent company. The legal capacity of 'pseudo-foreign company' was later detailed in the *Uberseering* case. Refer Case C-330/91 *The Queen v Inland Revenue Commissioners, ex parte Commerzbank AG* ('*Commerzbank*') [1993] ECR I-4017; Case C-1/93 *Halliburton Services BV v Staatssecretaris van Financien*, [1994] ECR I-1137.

1. The Union shall adopt measures with the aim of establishing or ensuring the functioning of the internal market, in accordance with the relevant provisions of the Treaties.
2. The internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties.

In so accomplishing this objective, the member states have agreed to exclude discriminatory measures on the ground of nationality (Article 18 TFEU (ex Article 12 TEC)) and prohibit regulatory measures which would impede the free movements guaranteed in the treaties. The freedoms guaranteed are free movement of goods (Articles 34-36 TFEU (ex Articles 28-30 TEC), services (Article 56-7 TFEU ex Articles 49-50 EC), persons (Article 45-8 TFEU ex Articles 39-42 EC), capital (Article 63(1) TFEU ex Article 56(1)) EC and the freedom of establishment (Article 49 TFEU ex Article 43 TEC).

The ASEAN Comprehensive Investment Agreement (ACIA) 2009 and the African Economic Community (AEC) are notable examples of investment agreements which resemble this feature. They contain similar objective. The preamble of ACIA emphasises the following:

‘Reaffirming the need to move forward from the AIA Agreement and the ASEAN for the Promotion and Protection of Investments signed in Manila, Philippines on 15 December 1987 (“ASEAN IGA”), as amended, in order to



further enhance regional integration to realise the vision of the ASEAN Economic Community (“AEC”)

The ASEAN Economic Community outlines that it will become a ‘single market and production base’. In order to achieve this, it comprises free flow of goods, free flow of services, free flow of capital and free flow of skilled labour.<sup>486</sup> In addition to that, the economic sectors are gradually liberalised, fortified with the protection of foreign investors via ACIA. Under ACIA, the main objective as stated in Article 1 is to ‘create a free and open investment regime’.

The African Economic Community (AEC) sets a similar standard. Article 2 of the AEC Treaty notes that

‘THE HIGH CONTRACTING PARTIES hereby establish among themselves an African Economic Community (AEC).’

The AEC provides freedom of establishment in Article 43 and free movement of capital in Article 45.

Similar to the EU incorporation of the non-discrimination principle to safeguard the fundamental freedoms and uphold the success of the EU economic integration, ACIA also includes the non-discrimination principle to promote and ensure the realisation of its economic integration objective. It is done by way of investment liberalisation and obliging all member states to provide national treatment to other

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<sup>486</sup> Declaration on the ASEAN Economic Community Blueprint, signed 20 November 2007, <<http://www.asean.org/news/item/declaration-on-the-asean-economic-community-blueprint>>, full version is available at <<http://www.asean.org/archive/5187-10.pdf>>, accessed on 21 September 2013.

states' investors and /or investments with respect to admission, establishment, acquisition, *etc* in their territories.<sup>487</sup> The principle of non-discrimination in the AEC is however only apparent in the most favoured nation principle in Article 37. It adopts a wider approach (includes any restriction) which would be covered under the general freedom of establishment and free movement of capital guaranteed by the treaty.

Generally, the 'negative integration' in the EU law in the context of the non-discrimination principle is similar to investment treaties as it includes areas which are not within the direct sphere of the EU law to regulate, such as direct taxation, but are left to the member states as long as they do not contradict the treaties.<sup>488</sup> It forms part of the 'decentralised' model of the common market in which the national regulatory autonomy is not interfered as long as the regulations are applied equally to home and host states' goods or persons.<sup>489</sup> This negative integration and decentralised model are made possible with the principle of non-discrimination.<sup>490</sup>

The logic of analogy is straightforward. The EU law grants free establishment of investments and free movement of investment capitals and thus obligates the member states to adhere to the non-discrimination principle. Similar to the effects of some investment treaties such as the ACIA, CAFTA-DR and to some extent NAFTA, the EU law encourages investments in other member states and prohibits

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<sup>487</sup> ACIA 2009, (n 471), Article 5.

<sup>488</sup> Case C-279/93 *Finanzamt Köln-Altstadt v Roland. Schumacker* ('Schumacker'), [1995] ECR I-225, para 21.

<sup>489</sup> Catherine Barnard, *The Substantive Law of the EU: The Four Freedoms* (3rd edn, OUP Oxford 2010) 18.

<sup>490</sup> The EU law regards the principle of non-discrimination as the first necessary step towards achieving an internal market. Sundberg-Weitman, *Discrimination on Grounds of Nationality* (n 475) 11.

the state to discriminate against them. Where it involves non-residents discriminated against residents,<sup>491</sup> it becomes akin to a national treatment situation in investment treaties. The ECJ in the *Truck Center* explicitly mentions the benefit of national treatment in the EU setting:

‘In the case of companies, it should be borne in mind that their registered office for the purposes of Article 58 of the Treaty serves, in the same way as nationality in the case of individuals, as the connecting factor with the legal system of a Member State. Acceptance of the proposition that the Member State of residence may freely apply different treatment merely by reason of the fact that the registered office of a company is situated in another Member State would deprive Article 52 of the Treaty of all meaning. Freedom of establishment thus aims to guarantee the benefit of national treatment in the host Member State, by prohibiting any discrimination based on the place in which companies have their seat (see *Test Claimants in Class IV of the ACT Group Litigation*, paragraph 43; *DenkavitInternationaal and Denkavit France*, paragraph 22; and Case C-284/06 *Burda* [2008] ECR I-0000, paragraph 77).’<sup>492</sup>

As for the reading from the EU perspective, Steffen Hindelang had made a connection between free movement of capital and freedom of establishment in the

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<sup>491</sup> It is pertinent to point that the EU law grants freedom not only to nationals of other member states but also to the nationals of the states themselves domestically. See *C-9/02 de Lasteyrie du Saillant* [2004] ECR I-2409 where the French tax was regarded by the ECJ as preventing its own citizens from transferring their residence abroad. Also, treating alike two different circumstances may also amount to discrimination.

<sup>492</sup> Case C-282/07 *Etatbelge-SPF Finances v Truck Center SA*, (*Truck Center Case*) [2008] I-10767, para 32.

EU law with national treatment.<sup>493</sup> He linked the situation of comparison between cross-border and domestic situations to the international law principle of ‘national treatment’.<sup>494</sup> Reference to the EU tax discrimination matters to ‘national treatment’ is also made by Tom O’Shea in his analysis of the concept of comparability and discrimination in the EU law.<sup>495</sup> The possibility of interaction between the EU law and international investment in the context of national treatment are also affirmed by some scholars within international economic law.<sup>496</sup>

There is no direct attempt to refer to the EU law in investment arbitration cases. Mentions however were made on the possibility of reference. Among those who noted the possible interactions were Thomas Walde and Federico Ortino.<sup>497</sup> Walde, in relating investment treaties to the ECJ (on the importance of protectionist element in discrimination cases) commented,

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<sup>493</sup> In his words with regard to free movement of capital; Art 56 EC (now A63 TFEU) also includes a prohibition of discrimination. If cross-border and domestic situations are compared, then this corresponds to the international economic law principle of national treatment. And he quoted P. Rudolf Dolzer from his book *Wirtschaft und kultur im Volkerrecht*. Hindelang, *The Free Movement of Capital and Foreign Direct Investment* (n 127) 129–135.

<sup>494</sup> Ibid 130. See generally: Juillard, ‘Freedom of Establishment, Freedom of Capital Movements, and Freedom of Investment’ (n 90).

<sup>495</sup> O’Shea, ‘Freedom of Establishment Tax Jurisprudence: Avoir Fiscal Re-visited’ (n 128). See also Philip Laroma, ‘Freedom of Establishment & EC Tax Law: The Case for ECJ consistency, Comparability: Consistent or Not Consistent?’ (Institute of Advanced Legal Studies 2009) 5 <[http://ials.sas.ac.uk/postgrad/courses/docs/MA\\_Tax\\_Working\\_papers/PHILIP\\_PUBLICATION\\_FI\\_NA.pdf](http://ials.sas.ac.uk/postgrad/courses/docs/MA_Tax_Working_papers/PHILIP_PUBLICATION_FI_NA.pdf)>, accessed on 28 January 2014.

<sup>496</sup> Walde, ‘Comments on the Discipline of ‘National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3); Walde and Kolo, ‘Investor-State Disputes: The Interface between Treaty-based International Investment Protection and Fiscal Sovereignty’ (n 461); J. H. H. Weiler, *The EU, the WTO and the NAFTA: Towards a Common Law of International Trade?* (Lindahl Lectures) (Oxford University Press, USA 2000); Stephan W. Schill, ‘Multilateralization through Interpretation: Producing and Reproducing Coherence in Investment Jurisprudence’ in *The Multilateralization of International Investment Law* (Cambridge University Press 2009).

<sup>497</sup> Walde, ‘Comments on the Discipline of ‘National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3); Ortino, ‘From “Non-Discrimination” to “Reasonableness”: A Paradigm Shift in International Economic Law?’ (n 63).

‘A similar approach would and has been used by the European Court of Justice to identify a discriminatory purpose of governmental measures. It is rather the effect than a particular individual intention which determines the finding of discrimination. While WTO cases deal with trade -not investment- and ECJ cases mainly with freedom of movement (which is mainly an issue of investment access), their (they are) by now very extensive and authoritative jurisprudence on discrimination cannot be ignored when issues of discrimination are raised under investment treaties.’<sup>498</sup>

The analogy between the EU and investment can be seen from the similar effect that both regimes have on the liberalisation of investments. The EU jurisprudence of freedom of establishment and free movement of capital facilitate investment opportunities for the nationals of the EU member states to pursue establishment of investments in another member state. By freedom of establishment in Article 49 of the Lisbon Treaty, the member states are prohibited from restricting nationals of another member state to establish or manage their undertakings in the state. Article 49 TFEU reads:

‘... restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.

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<sup>498</sup> Walde, ‘In the Arbitration under Article 26 Energy Charter Treaty (ECT), *Nykomb v. The Republic of Latvia*-Legal Opinion’ (n 170) para 41.

Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the Chapter relating to capital.’

This provision allows nationals of a member state to self-employ or set up companies in another member state. It is a broad fundamental freedom allowing efficient allocation of production factors in the EU including goods, services and capital. It obliges member states to allow nationals of the other member states to participate in a ‘stable and continuous basis’<sup>499</sup> in the economic life<sup>500</sup> of the host state. The freedom of establishment involves the actual pursuit of an economic activity through a fixed establishment in another Member State for an indefinite period.<sup>501</sup> These characteristics are similar to the characteristics of foreign investments generally covered in investment treaties as investments must be of ‘certain duration’.<sup>502</sup>

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<sup>499</sup>Case C-55/94, *Gebhard* [1995] ECR I-4165, para 25.

<sup>500</sup>In the case of Case 2-74 *Jean Reyners v Belgian State* [1974] ECR 00631, the court elaborated that freedom of establishment within the sphere of activities as self-employed persons is intended to oblige member states to facilitate effectively the economic and social interpenetration of nationals of the other member state within the community of the host state.

<sup>501</sup>Case C-221/89 *The Queen v Secretary of State for Transport, ex parte Factortame Ltd and others* [1991] I-03905 (*Factortame* case), para 20-22; the registration of a vessel was regarded as an exercise of freedom of establishment as it serves as a vehicle for the pursuit of economic activity that includes fixed establishment in the State of registration.

<sup>502</sup>*Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction, 31 July 2001, para 54.

This is similar to treaties which grant the right of access, commonly by way of the national treatment or most favoured nation provisions. The ACIA provides freedom of establishment by way of granting non-discrimination in the pre-establishment of investments. Article 5 (1) of ACIA reads:

‘Each Member State shall accord to investors of any other Member State treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the admission, establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments in its territory.’<sup>503</sup>

Similar language can be found in Article 10.3 of CAFTA-DR, Article 3 in the 2004 US-Model BITs, Article 3(1) of the 2003 Canadian Model BIT, the Japanese Model BITs and NAFTA.<sup>504</sup> By granting right of access, the host states are prohibited from discrimination from the establishment stage of foreign investments in the host states. Apart from regional trade or investment treaties, a country adopting mutual national treatment model which grants a common regime of entry and establishment within the states, creates the same effect as the freedom of establishment as in the TFEU.<sup>505</sup> With regards to the German BITs, although it does not explicitly contain the right of establishment, it was suggested by Sandrock that it exists nevertheless via two methods, firstly by way of the interpretation of ‘investment’ and ‘investor’ and secondly via German administrative law of subjective public rights that eventually

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<sup>503</sup> Article 5(2) ACIA 2009 provides similar protection for ‘investments’.

<sup>504</sup> NAFTA, Article 1102.

<sup>505</sup> P. Gugler and V. Tomsik, ‘The North American and European Approaches in the International Investment Agreements’ (2007) 4 Transnational Dispute Management (TDM) 12 <<http://www.transnational-dispute-management.com/article.asp?key=1082>>, accessed on 28 January 2014.

lead to the same effect of access.<sup>506</sup> Sandrock's argument could be to some extent reflecting other BITs as the restrictions imposed by host governments prior entry are normally administrative in nature, and what foreign investors should do is to comply with the requirements. Once the requirements are complied with and the investments are admitted, the investments enjoy the permanent presence of the investments to carry out their economic activities.<sup>507</sup>

As for other investment treaties which adopt the post establishment approach, this freedom is extended once the investments have entered into the host states. China, Hong Kong<sup>508</sup> along with other European BITs regulates access of foreign investors in their treaties.<sup>509</sup> BITs of this kind allow admission of investments 'in accordance to the law'.<sup>510</sup>

As far as free movement of capital is concerned, Article 63 of the TFEU provides that 'all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.' This article, which came later in the EU jurisprudence, is an outcome of progressive advancements to liberate

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<sup>506</sup>Sandrock, 'The Right of Foreign Investors to Access German Markets: The Meaning of Article 2(1) of the German Model Treaty for the Promotion and Protection of Foreign Investments' (n 340).

<sup>507</sup>The correlations between freedom of establishment as a well-settled concept and freedom of investment is attempted by Juillard in his article. The two are not synonymous, but related. See Juillard, 'Freedom of Establishment, Freedom of Capital Movements, and Freedom of Investment' (n 90) 333.

<sup>508</sup>Zeng Huaqun, 'Initiative and Implications of Hong Kong's Bilateral Investment Treaties' [2010] *The Journal of World Investment & Trade* 2.

<sup>509</sup>Berger, 'China's New Bilateral Investment Treaty Programme: Substance, Rational and Implications for International Investment Law Making' (n 166); Gugler and Tomsik, 'The North American and European Approaches in the International Investment Agreements' (n 505).

<sup>510</sup>The nature of European BITs in adopting investment control is also referred to as 'European approach towards FDI regulation' or BITs containing 'admission clause'. See Julien Chaisse, 'Promises and Pitfalls of the European Union Policy on Foreign Investment—How Will the New EU Competence on FDI Affect The Emerging Global Regime?' [2012] *Journal of International Economic Law* <<http://jiel.oxfordjournals.org/content/early/2012/02/20/jiel.jgs001>>, accessed on 28 January 2014.



movement of capital. The coverage nomenclature of capital movements in the European Union law is broad and it includes direct investments.<sup>511</sup>

Similarly, most investment treaties incorporate provisions on free transfer of fund which enables investors to bring in and out capital and profit from the host state. The Netherlands-India BIT for instance provides:

‘Repatriation of Investment and Returns

(l) Each Contracting Party shall assure to investors of the other Contracting Party, without delay and on a non-discriminatory basis, the unrestricted transfer inter alia of:

(a) Capital and additional capital amounts used to maintain or increase investments;

(b) Net operating profits including dividends and interest;

(c) Repayments of any loan including interest thereon, relating to the investments;

(d) Payment of royalties and service fees as far as it is related to the investment;

(e) Proceeds of sales or liquidation of the investment;

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<sup>511</sup> Of other aspects, it includes personal funds, real estate investments or purchases, securities investments and granting of loans and credits. This is contained in Directive 88/361 of June 24, 1988 which was earlier adopted in Article 73b(1) EC (The Maastricht Treaty) and Article 56(1) EC (Amsterdam Treaty). Directive No.88/361 is still referred to by the ECJ despite it being significantly reproduced in the treaties. It was said to have the same indicative value in the case of *Trummer and Mayer*. See Case C-222/97 *Manfred Trummer and Peter Mayer* [1999] ECR I-1661. The directive gave full liberalisation of capital to the European Community with transitional arrangements for some member states.

(f) The earnings of nationals of one Contracting Party or of any third state who work in connection with investments in the territory of the other Contracting Party.

(2) Currency transfer under paragraph (1) shall be in a freely convertible currency. Such transfers shall be made at the prevailing market rate of exchange on the date of transfer.’<sup>512</sup>

This model of the right of transfer of funds provision is common in many investment treaties, such as in the Article 6 of Mongolia-Korea BIT,<sup>513</sup> Article 45 of the AEC and Article 13 of ASEAN (ACIA). It provides an unrestricted effect of transfer of fund, thus result to a huge effect of protection to foreign investors. There are some investment treaties however which provide reservations such as the India-Malaysia BIT which guarantees free transfer of fund ‘subject to its law, regulations and national policies’.<sup>514</sup> Be that as it may, there is still a substantial level of freedom of movement of capital that is granted by the right of transfer of fund in the investment treaties, and the law, regulations and national policies must be construed strictly so as not to impede unjustifiably the essence of the freedom. Capital inflows in both the EU and investment face similar threats of restrictions including exchange restrictions, capital account transactions and international payment or transfer. By providing that each party shall assure to investors of the other Contracting Party without delay and on a non-discriminatory basis the unrestricted transfer of funds/capital, the BITs are actually seeking to ensure the competitiveness of foreign

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<sup>512</sup> Article 7, Netherlands- India BIT, signed 6 November 1995 , entry into force 1 December 1996, < [http://unctad.org/sections/dite/ia/docs/bits/netherlands\\_india.pdf](http://unctad.org/sections/dite/ia/docs/bits/netherlands_india.pdf)>, accessed 21 September 2013.

<sup>513</sup> Mongolia – Korea BIT, signed 28 March 1991, < [http://unctad.org/sections/dite/ia/docs/bits/korea\\_mongolia.pdf](http://unctad.org/sections/dite/ia/docs/bits/korea_mongolia.pdf)>, accessed 24 September 2013.

<sup>514</sup> Article 6, India-Malaysia BIT, signed 3 August 1995, entry into force 12 April 1997, [http://unctad.org/sections/dite/ia/docs/bits/India\\_Malaysia.pdf](http://unctad.org/sections/dite/ia/docs/bits/India_Malaysia.pdf), accessed 21 September 2013.

investor/investment. It must be noted that similar issues revolve in the EU law. Within the EU member states, capital integration is also regarded as a challenging progress as it involves sensitive domestic political concerns and economic policies. Thus, even when eventually the EU member states agreed on the direct effect of free movement of capital, there are still various justifications that the member states attempted to seek when their regulatory measures are challenged as evidenced in the decided cases.<sup>515</sup>

This is where the learning process is essential. The investment law could learn from the vast case laws from the EU jurisprudence. Especially in the context of ACIA where no case so far has been brought,<sup>516</sup> it is key responsibility of the arbitrators to decide the direction of interpretation. In the context of freedom of establishment for instance, there are many case laws where national legislations were challenged for infringement of the freedom.<sup>517</sup> Analogy to the EU law helps the international

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<sup>515</sup>The dilemma around Article 63 is even more so as it has an *erga omnes* effect, which extends the right to third countries. Being aware of the huge scope of this freedom and the sensitivity of capital taxation to domestic economy, the TFEU provides exceptions on third countries and on other general grounds such as in tax treatment and prudential supervisions or public policy and security under very specific circumstances, see Article 64(1) and 65 TFEU.

<sup>516</sup> However, there was a case under the 1987 ASEAN Treaty for Promotion and Protection of Investments (before the entry of ACIA) which is worth noting. The tribunal in that case eventually found lack of jurisdiction. See *Yaung Chi Oo Trading Pte Ltd., v Government of the Union of Myanmar*, Association of Southeast Asian Nations (ASEAN) Arbitral Tribunal, ASEAN I.D. Case No. ARB/01/1, Award, 31 March 2003 (42 ILM 540 (2003)). See also elaboration of the case in Lay Hong Tan, 'Will ASEAN Economic Integration Progress Beyond a Free Trade Area?' (2004) 53 *International & Comparative Law Quarterly* 935.

<sup>517</sup> The case of *Avoir Fiscal* in 1983 marked a significant era in the development of freedom of establishment of companies in the EU law. It progressed further with the decisions of landmark cases which imposed national legislations or established principles to respond to, such as *Centros*'s 'seat doctrine' and *Bachman*'s 'fiscal cohesion defense'. By the decisions in many FoE cases, the ECJ has indirectly 'fashioned' the landscape of member states' tax policies. This portrays the significant role of the non-discrimination principle in the negative integration of the EU law. The member states have to eventually tailor their internal tax system following the decisions based on the basic rule that even though direct taxation is a matter of competence within the member states, it must be exercised consistent with the EU law. See Eddy Wymeersch, 'Centros: A Landmark Decision in European Company Law' [1999] *Financial Law Institute Working Paper* 99-15 <[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=190431](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=190431)> , accessed on 29 January 2014. For cases, see *Marks & Spencer*, paragraph 29; Case C-374/04 *Test Claimants in Class IV of the ACT*

investment regime to analyse the impact of the approaches taken by ECJ. Where the approach is suitable to the investment context, they may be instructive to the arbitrators.<sup>518</sup>

### 3.0 Like Situations

The EU law acknowledges that the guiding methodology in discerning discrimination is by comparing claimants with a comparator in the same situation. In the case of *Test Claimants* the court re-emphasised this requirement,

‘In order to determine whether a difference in tax treatment is discriminatory, it is, however, necessary to consider whether, having regard to the national measure at issue, the companies concerned are in an objectively comparable situation.’<sup>519</sup>

Despite the huge volume of cases on discrimination, the EU jurisprudence does not have a certain criteria of likeness (or criteria associated to likeness) similar to that can be found in the GATT/WTO.<sup>520</sup> This in a way provides a level of flexibility to the ECJ in deciding what constitute like situations of the comparators. Nevertheless,

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*Group Litigation* [2006] ECR I-11673, paragraph 36; and Case C-182/08 *GlaxoWellcome* [2009] ECR I-0000, paragraph 34.

<sup>518</sup> Roberts, ‘Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System’ (n 322).

<sup>519</sup> Case C-374/04 *Test Claimants in Class IV of the ACT Group Litigation v Comm’rs of Inland Revenue*, [2006] ECR I-11,673. See also *Schumacker*, (n 488), para 30 and Case C-311/97 *Royal Bank of Scotland* [1999] ECR I-2651, para 26.

<sup>520</sup> The tests are the characteristics test, the competitive and substitutability test, the aims and effects test and the PPM. Refer to Ch.3 for more discussion.

the ECJ managed to highlight certain principles in discerning discrimination judging from the case laws.<sup>521</sup> This section will extract the principles from the jurisprudence.

#### 4.1 'Situation' as Paramount Consideration

The emphasis on the 'situations' of the comparators is obvious and paramount in free movement of capital and freedom of establishment cases, that even the most established principles could be put to second. The 'seat doctrine' in company law for instance was put in controversy in the *Centros* case.<sup>522</sup> Another example is, by providing equal treatment in the annual income tax assessment to non-residents in direct taxation, it deviates from the normal international tax practice which would normally be granted on a reciprocal basis to non-residents by way of Double Taxation Treaties.<sup>523</sup> This would otherwise be reserved within the sphere of the host states in international investment law and would likely be justifiable for discriminatory treatment. In general, the Court would accept objective differences in given circumstances.<sup>524</sup>

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<sup>521</sup> On the contrary, there are critiques by scholars due to the variation of reasoning by the ECJ in a number of cases. Mason & Knoll regarded discrimination on tax cases as the following:

'Determining whether taxpayers are similarly situated is therefore crucial for determining whether there is discrimination. But the ECJ has not provided clear guidance on when resident and nonresident taxpayers are similarly situated, such that they must be taxed the same way, and when they are not. The resulting collection of decisions is a hodgepodge, lacking any clear set of guiding principles.'

Ruth Mason and Michael Knoll, 'What Is Tax Discrimination?' [2012] Faculty Scholarship, University of Pennsylvania Law School 1030. See also Dennis Weber, 'The Bosal Holding Case: Analysis and Critique' (2003) 4 EC Tax Review 220; Michael J Graetz and Alvin C Warren Jr., 'Income Tax Discrimination: Still Stuck in the Labyrinth of Impossibility' (2012) 121 The Yale Law Journal.; Alvin C Warren and Michael J Graetz, 'Income Tax Discrimination and the Political and Economic Integration of Europe' (2006) 115 Yale Journal of International Law 1186.

<sup>522</sup> Eva Micheler, 'The Impact of the Centros Case on Europe's Company Laws' (*The Company Lawyer*, June 2000). See Case C-212/97 *Centros Ltd v Erhvervs- og Selskabsstyrelsen* [1999] I-01459.

<sup>523</sup> *Schumacker* (n 488). See also O'Shea, 'Taxation of Non-Residents' (n 128).

<sup>524</sup> In the *Truck Centre case*, the court took into consideration the capacity of the state that affects the situation of the comparators. *Truck Center Case*, (n 492), para 42. See also Mady Werner, 'Analysis of the ECJ's Recent Judgment in Case C282/07, *Etat belge-SPF Finances v Truck Center*' (2009) EC Tax Students' Conference Institute of Advanced Legal Studies <[http://ials.sas.ac.uk/postgrad/courses/docs/MA\\_Tax\\_Working\\_papers/Mady\\_PUBLICATION\\_FIN\\_AL.pdf](http://ials.sas.ac.uk/postgrad/courses/docs/MA_Tax_Working_papers/Mady_PUBLICATION_FIN_AL.pdf)>., <[http://ials.sas.ac.uk/postgrad/courses/MA\\_tax\\_law\\_workingpapers.htm](http://ials.sas.ac.uk/postgrad/courses/MA_tax_law_workingpapers.htm)>, accessed on 23

As a general rule in direct taxation, the situations of residents and non-residents are not comparable.<sup>525</sup> This is found in the international tax law principles of residence and territoriality which are adopted by most national laws. According to these principles, residents are taxed based on their worldwide income while non-residents are taxed on their acquired income within the territory. This renders the incomparability of residents and non-residents in taxation. However, with the implementation of the EU law which seeks for free movement of factors of production, conflicts are found with the grounded international tax practice known among the member states. There is no clear rule which take precedence of this incomparability, but case laws have suggested incomparability can only be the case if member states can prove it objectively. To prove the objectivity of a discriminatory measure, the situations of the comparator is key.

As far as companies are concerned, nationality of a company is determined based on its seat of establishment. Resident and non-resident companies are as a rule non-comparable. If the court, by construing the measure in light of the discriminatory effect it cause to the non-resident companies in comparison to resident companies which are in like circumstances which could undermine the *effet utile* of the EU law, the court could deviate from this general rule. The ECJ in the case of *Commission v*

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September 2013; O'Shea, 'Truck Center: A Lesson in Source vs. Residence Obligations in the EU' (n 128), <<http://www.ccls.qmul.ac.uk/docs/staff/oshea/52215.pdf>> , accessed 23 September 2013.

<sup>525</sup> *Schumacker* (n 488), para 31, *D v Inspecteur van de Belastingdienst/Particulieren/Ondernemingenbuitenlandte Heerlen*, para 28. It must be noted that in respect of comparability, the EU law deals with comparison between different sets of comparators-residents and non-residents, among two residents or among two non-residents located inside and cross border. The one which is similar to the national treatment concept and coverage in international investment treaties is involving residents and non-residents as in most cases discrimination against non-residents also means discrimination against other nationalities. This nevertheless does not render other comparisons irrelevant. The principles derived from the courts deliberation on the comparison could still be applied by analogy to non-nationals, similar to how analogy of important principles on discrimination from personal tax or inheritance cases.

*France (Avoir Fiscal)* emphasised that residence could not always be the differentiating factor. The court made an important observation:

‘Acceptance of the proposition that the member state in which a company seeks to establish itself may freely apply to it a different treatment solely by reason of the fact that its registered office is situated in another member state would thus deprive that provision of all meaning.’<sup>526</sup>

If by such differentiation it leads to overt or covert discrimination, it will still be impeding the EU law. The result of discrimination can only be seen if two companies of the same situations are compared. In the case of *Sotgiu*, the court mentioned to this effect,

‘...that the rules regarding equality of treatment forbid not only overt discrimination by reason of nationality or, in the case of a company, its seat, but all covert forms of discrimination which, by the application of other criteria of differentiation, lead in fact to the same result.’<sup>527</sup>

The situation of the comparators was articulated in the case of *Bouanich* highlighting that if the difference of treatment occurs out of an occasion, the occasion must be objectively justified. In the case of *Bouanich*, the Swedish legislation was challenged for discriminating against non-resident shareholders with regards to the repurchase of shares. The repurchase of shares by residents was taxed as a capital gain and deducted for the cost of acquisition but was regarded as a distribution of a dividend

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<sup>526</sup> *Avoir Fiscal Case*, (n 464), para 18.

<sup>527</sup> Case 152/73 *Sotgiu v Deutsche Bundespost* [1974] ECR 153, para 11.

amounting to no deduction. This results to tax advantage for resident shareholders. In construing likeness of the resident and non-resident shareholders in this case, the court found that had it not been because of the action of repurchase of shares, the two residents are considered in like circumstances. The point of comparability falls on ‘the occasion of the purchase of the share’ and the court did not see any objective reason to justify the discrimination, as there was nothing extraordinary but a repurchase of shares. The court concluded the existence of an arbitrary discrimination.<sup>528</sup> Thus, two comparators which are otherwise similar can be in a different situation because of an occasion. However, justification of that occasion is essential.

In another case, the court ruled that if an objective situation is relied upon for a discriminatory treatment, that discriminatory treatment must be effective to achieve the intended objective situation. In the case of *Manninen*, tax credit was granted by the Finnish government to compensate for double taxations.<sup>529</sup> The compensation was limited to dividends received from domestic corporations. As a result of this, revenue from capital of non-Finnish origin receives less favourable tax treatment than dividends distributed by companies established in Finland. Although Finland has attempted to draw the difference of character between the companies – claiming that Finnish companies are already subjected to corporation tax which in turn entitles the shareholders for tax credit- the court urged to construe the situations at hand. The court concluded that the shareholders fully taxable in Finland (regardless of whether receiving dividends from a foreign or domestic company) eventually found themselves in a comparable situation because they are equally exposed to double

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<sup>528</sup> Case C-265/04 *Margaretha Bouanich v Skatteverket* [2006], paras 38-41.

<sup>529</sup> Case C-319/02, *Manninen*, [2004] ECR I-7477, para 13.



taxation. When Finland relied on the justification of compensating for double taxation, there is no reason to deprive a shareholder receiving dividends from another member state if they equally face the risk of double taxation.

Another method of construing ‘situation’ is by looking at the legal position of the comparators. If the position of the law is similar in covering the comparators, there is no objective reason to discriminate them. In the existence of a specific legal provision that groups the comparators in like situation, the court is reluctant to accept justifications to group them apart. This is also termed as ‘legal comparability’<sup>530</sup> as the position of the law governing the parties is examined of which similarity is derived.<sup>531</sup> In the case of *Commission v France (Avoir Fiscal)*, since the companies were treated the same way for the purpose of taxing the profits, there is no objectivity on the discriminatory measure when it comes to the granting *avoir fiscal* later. France has admitted that there is no objective difference relating to the treatment.<sup>532</sup> Similarly, in the case of *Arens-Sikken*, the court highlighted that by providing similar treatment in inheritance of both categories of persons under comparison the same way for the purpose of tax, there is no objective difference between them.<sup>533</sup>

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<sup>530</sup> Refer to Michael Lang, ‘Recent Trends in ECJ Case Law in the Area of the Freedoms and Direct Taxation’, <[https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0CC8QFjAA&url=https://www.ibdt.com.br%2Fmaterial%2Farquivos%2FAtas%2FIBDT\\_10\\_June\\_2010\\_ECJi.ppt&ei=uhDpUqKiI6v07Abk7IC4CA&usg=AFQjCNE\\_I0yTQTbrTZxPzOtTTiMqKGPvag&sig2=4YiZQm2WGSMj6AS24HzFDg](https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0CC8QFjAA&url=https://www.ibdt.com.br%2Fmaterial%2Farquivos%2FAtas%2FIBDT_10_June_2010_ECJi.ppt&ei=uhDpUqKiI6v07Abk7IC4CA&usg=AFQjCNE_I0yTQTbrTZxPzOtTTiMqKGPvag&sig2=4YiZQm2WGSMj6AS24HzFDg)> accessed on 28 January 2014.

<sup>531</sup> See also Case C-11/07 *Hans Eckelkamp and Others v Belgische Staat* [2008] I-06845, para 63 and Case C-170/05 *Denkavit Internationaal and Denkavit France* [2006] ECR I-11949, paragraph 35.

<sup>532</sup> *Avoir Fiscal*, (n 464), para 20.

<sup>533</sup> Case C-43/07 *D.M.M.A. Arens-Sikken v Staatssecretaris van Financiën* (*‘Arens-Sikken’*), [2008] ECR I-0000.

The next method is by construing the factual differences of the comparators. In the case of *Schumacker*, the ECJ took cognisance of the factual differences between the residents and non-residents which overrides the general rule of non-comparability of the two categories of persons.<sup>534</sup> The Germany income tax law applied different tax regimes to peoples under these classifications in which residents are subject to tax on all their income ('unlimited taxation') while non-residents in Germany are subject to tax only on the part of their income arising in Germany. By this arrangement, non-residents are deprived from having their annual wages tax adjustment made by the employer and from the annual income tax assessment by the administration. This consequently could not qualify them for reimbursement of any overpaid tax at the end of the year. Although Germany put forth the rationales of difference of treatment of non-residents based on the territoriality argument assuming that generally the income received in the member state is only part of the total income (the rest of which will be taxed at the place of residents), it was observed in this case that the claimant has no income derived from his state of residence and thus results to his personal and family circumstances are taken into account neither in the state of residence nor in the state of employment. The court took cognisance of this situation and did not uphold Germany's concern of non-residents enjoying tax benefits in both States.<sup>535</sup> The court deviated from the general rule of non-comparability of residents and non-residents due to the non-objectivity of the host state reasons maintaining the rule and in corresponding to the particular circumstances of the claimant. The court consistently decided in the case of *Gschwind*, that there was comparability as the claimant did received substantial income from his State of residence.<sup>536</sup>

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<sup>534</sup> *Schumacker*, (n 488), para 40.

<sup>535</sup> *Ibid.*

<sup>536</sup> *Case C-391/97 Gschwind* [1999] ECR I-5451.

Lastly, it is notable that the court took cognisance of the reliance on previous preferential treatment accorded by the member state. In the case of *Commerzbank*, the justification brought by the member state was that because non-residents enjoy privileged treatment in not having to pay tax normally paid by resident companies, they therefore were not entitled to repayment supplement. The ECJ held that:

‘The fact that the exemption from tax which gave rise to the refund was available only to non-resident companies cannot justify a rule of a general nature withholding the benefit. That rule is therefore discriminatory.’<sup>537</sup>

This entails that if a member state relies on a previous preferential treatment created for non-nationals it would be discriminatory to treat unfavourably on a general nature based on that difference.

#### *4.2 The Principle of ‘Effet Utile’ and Likeness*

It is observed that the finding of likeness need not necessarily be in the form of stand-alone criteria which are applied in different sets of circumstances, but could be a principle that is inherent in all cases. The important principle that the ECJ collaterally took cognisance of is the principle of ‘*effet utile*’.

The principle of *effet utile* is also termed as the doctrine of effectiveness. Applying this doctrine, the adjudicator would construe the design and purpose of the legislation and the effects it sought to achieve. This is how the court would fill in a

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<sup>537</sup> Case C-330/91 *The Queen v Inland Revenue Commissioners, ex parte Commerzbank AG* [1993] ECR 1993 I-04017 para 19.

gap as a teleological method of interpretation.<sup>538</sup> Walde regarded the principle of effectiveness as a key principle of interpretation which can be used ‘to create a presumption against an interpretation which leaves no meaning or effect to a particular textual element’.<sup>539</sup>

The EU law imposes a strict approach in tolerating justifications for discriminations by member states. It constantly emphasises the *effet-utile* or useful effect to its *raison d’être* of the EU law; i.e. achieving an internal market. The catalyst of the prohibition of discrimination is that it protects the functioning of the EU internal market. Thus, if a member state introduces a discriminatory measure, the test is also whether the measure hinders or restricts the realisation of the EU freedoms as guaranteed in an internal market or likely discourages cross-border economic activities.

The use of *effet-utile* is especially very apparent in the areas in which the EU has no direct regulation such as in direct taxation.<sup>540</sup> In the case of *Cadbury Schweppes*, a national measure is not justified if it relates to a justification sought to circumvent the application of the legislation of the state concerned.<sup>541</sup> In the case of *Amministrazione delle Finanze dello Stato v Simmenthal SPA*,<sup>542</sup> the ECJ held that :

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<sup>538</sup> Nial Fenelly, ‘Legal Interpretation at the European Court of Justice’ (1996) 20 Fordham International Law Journal 674.

<sup>539</sup> Thomas W Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP Oxford 2009) 738.

<sup>540</sup> This includes cross-border inheritance taxation. See Case C-513/03, *Van Hilten-Van der Heijden* [2006] I-01957.

<sup>541</sup> C-196/04 *Cadbury Schweppes plc and Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue* [2006] I-07995, para 76.

<sup>542</sup> Case 106-77 *Amministrazione delle Finanze dello Stato v Simmenthal SPA* (No 2) (1978) 3 CMLR 263, para 17.

‘It must be pointed out in that regard that the requirement of non-discrimination laid down by the Court cannot be construed as justifying legislative measures intended to render any repayment of charges levied contrary to Community law virtually impossible, even if the same treatment is extended to taxpayers who have similar claims arising from an infringement of national tax law. The fact that rules of evidence which have been found to be incompatible with the rules of Community law are extended, by law, to a substantial number of national taxes, charges and duties or even to all of them is not therefore a reason for withholding the repayment of charges levied contrary to Community law.’

The ECJ has been very firm in the *effet-utile* of the integration. The non-discrimination principle does not function solely to achieve this aim but is supported by the fall back general prohibition of restriction where the requirements to fulfil a discrimination case is not met.<sup>543</sup>

However, in order to apply this principle in the investment context, caution must be made to the EU experience as to the restrictive effect of discrimination cases.

Discrimination analyses are often prematurely concluded on the *effet-utile* basis.<sup>544</sup>

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<sup>543</sup>It is regarded as a two prong investigation, as in *Gebhard* (n 499), Case C-250/95 *Futura Participations and Singer* [1997] ECR I-2471 and *Truck Center Case* (n 492). The fact that restrictions can still occur if the regulation is not discriminatory is referred to as the drawback of discrimination tests. Especially in the context of free movement of goods and services, the market access test is alternatively applied to identify regulatory measures that constitute restriction or hindering the market access. See Barnard, *The Substantive Law of the EU* (n 489) 19; Gabrielle Pizzuto, ‘Restriction Analysis in ECJ Tax Jurisprudence Relating to the Freedom of Establishment: Is the Court Reinventing the Wheel?’ (2009) EC Tax Students’ Conference Institute of Advanced Legal Studies <[http://ials.sas.ac.uk/postgrad/courses/MA\\_tax\\_law\\_workingpapers.htm](http://ials.sas.ac.uk/postgrad/courses/MA_tax_law_workingpapers.htm)>., <<http://ials.sas.ac.uk/postgrad/courses/MA tax law workingpapers.htm>>, accessed on 23 September 2013.

<sup>544</sup>It is said to be too easy to conclude a discrimination case Ruth Mason, ‘A Theory of Tax Discrimination’ [2006] NYU Jean Monnet Working Paper No. 09/06

Literatures have also commented that this is an emerging approach in the EU tax cases, known as the ‘restrictive discrimination’ approach.<sup>545</sup> In the EU cases, the discussions are not constructed separately, and thus one would find that the restriction test is applied almost naturally with the discriminatory assessment.<sup>546</sup>

Technically, differing to the EU law, the discussion of the national treatment in investment treaties is placed as a separate substantive claim. The question of restriction is not invoked in national treatment, although substantively, the claimant may resort to fair and equitable treatment as a fall back claim in the event if national treatment claim is not satisfied. The investment treaties do not extend to prohibit all restrictive measures which hinder foreign investment, thus adopting the restrictive approach in lieu of discrimination would render excess of jurisdiction of the claims.

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<[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=978880&download=yes](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=978880&download=yes)>, accessed on 29 January 2014.

<sup>545</sup> Mattias Dahlberg, ‘The European Court of Justice and Direct Taxation: A Recent Change of Direction?’ in Krister Andersson, Eva Eberhartinger and Lars Oxelheim (eds), *National Tax Policy in Europe* (Springer Berlin Heidelberg 2007) . On the account of judicial philosophy, the EU law is commented heavily on the direction of justice and values adopted in the jurisprudence. It has been argued that the EU law construes justice as ‘economistic nature of justice’ as opposed to the ‘perceived notion of justice’. See Williams, ‘Promoting Justice after Lisbon’ (n 484); Williams, ‘Taking Values Seriously’ (n 484). This is due to the establishment of the EU which was heavily grounded on the economic ideas. See Allott, *The Health of Nations* (n 482) 258. Allot agreed that the economic philosophy was the ‘aggregate economic phenomena’. This can also be seen from the economic oriented aims from the Single European Act in 1987 to the recent Lisbon Treaty.

<sup>546</sup> Another way of looking at this phenomenon is by referring it as an ‘elaborated discrimination’ approach which maintains the importance of the principle of non-discrimination in EU law. The argument is that if the analysis is taken over by the restrictive approach, the consequence is that every measure introduced by member states would be a restriction and have to be adjudicated. It is also important to bear in mind that member states possess tax sovereignty and thus they deserve to introduce measures for the national interest provided that they are objectively reasoned. In the absence of any harmonisation, the member states can by way of bilateral agreements prevent double taxation by allocating powers of taxation among themselves (see Case C-307/97 *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt* [1999] ECR I-06161, para 57. See also Case C-336/96 *Gilly* [1998] ECR I-2793, paras 24 and 30 [1999] ECR I-6161, paragraph 57). By elaborated discrimination, it suggests that the interpretation of discrimination is extended to the objectivity of the measure adopted to the *effet-utile* of the EU treaties. This is true as in most of the cases, the courts took the approach of determining comparability of the situations and the objectivity of such comparability. This second observation provides more sense as a proper analysis of discrimination would naturally require the objectivity of the comparison so as to justify the comparability, hence the ‘elaborated discrimination’.

Thus the effect of restrictive reading of the non-discrimination treatment would highly likely occur in the EU context, and less likely in investment law.<sup>547</sup>

#### *4.3 Other observations on the Determination of Likeness*

The first observation is the narrowness of the scope of examination. It is important to note that in so comparing the EU jurisprudence of free movement of capital and establishment to the investment law, one would notice that the EU law does not construe the physical/ tangible aspects of the subjects of investments as in investment tribunal. There is no reference of the economic sector as a criterion of likeness in the EU jurisprudence.<sup>548</sup> This is due to the nature of grounds of actions in both jurisprudences. On the other hand, the national treatment provision in investment treaties is a separate substantive claim which requires the tribunal to assess likeness from the very type or nature of the investments. Determining the economic sector of the investments is a preliminary assessment of likeness in investment law. In the EU law on the other hand, the claims are brought under free movement of capital and freedom of establishment and thus comparison is conducted directly on the aspect of capital and establishment. Thus, the narrow scope of comparison in the EU law does not mean that it ignores other elements/criteria of likeness, but because the EU discrimination assessment does not require so.

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<sup>547</sup> The restrictive effect by the application of unguided *effet utile* is anticipated. Thus, the principle should be exercised in ‘great care’ taking into account the overall policies, so as not to ‘make the treaty and its elements more effective than they appear on paper on the assumption that this is what the parties (and the Vienna Rules) wanted?’ See Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ (n 539) 739.

<sup>548</sup> In the case of *Avoir Fiscal* (n 464), there was an indication that the comparison was made within the insurance sector, but the emphasis was not insurance as a sector but the legal positions in the insurance sector which turned the examination on the legal situations of the comparators.

Despite the narrow scope of comparability, it enables the ECJ to explore the potentials of the circumstances within the context of establishment and movement of capital between the comparators. This allows scrutiny on how a measure would impact on comparators from the two viewpoints. Investment law benefits from this process because establishment and capital movement are significant elements of investment. It is observed that the investment tribunals should take cognisance of these aspects towards a more investment approach of analysis as compared to the heavily trade approach of characteristic examination which may only be relevant to the preliminary assessment of likeness in determining the economic sector.

Secondly, it is observed that justification arguments are often found occurring at the comparability level.<sup>549</sup> In the *Blanckaert* case for instance, the member state claimed the cohesion of its tax system as the justification of the discriminatory treatment. The member state insisted that there is an objective difference between a non-resident taxpayer who is not insured under the Netherlands social security system and a resident who is insured. Contrary to the non-residents, the residents are liable, as a rule to pay contributions under that system. The court construed this justification in assessing the likeness of the situation of the comparators and concluded:

‘The answer to the first question must therefore be that Articles 56 EC and 58 EC must be interpreted as not precluding a law of a Member State under which a non-resident taxpayer who receives income in that State only from

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<sup>549</sup>Recent cases of the EU are those cases from 2005 onwards, following the analysis of trends in ECJ case law in the area of the freedoms and direct taxation by Michael Lang. The cases are grouped in several phases – before 1986 where there were no tax cases, between 1986-2005 which marked the EU restrictive approach in accepting justifications by member states and from 2005 onwards where ECJ started to give emphasis on, inter alia, proportionality and construing justification at comparability level.



savings and investments and who is not insured under the social security system of that Member State cannot claim entitlement to tax credits in respect of national insurance, whereas a resident taxpayer who is insured under that social security system is entitled to those credits when his taxable income is calculated, even if he receives only income of that same kind and does not pay social security contributions.<sup>550</sup>

Similar approach is taken in other cases such as the *Truck Centre* case<sup>551</sup> and *D. v Inspecteur van de Belastingdienst*.<sup>552</sup> In the case of *D*, the member state justified its discriminatory treatment by the existence of a bilateral tax convention for avoidance of double taxation which only extends to residents to the other state party to the convention. The court mentioned,

‘The fact that those reciprocal rights and obligations apply only to persons resident in one of the two Contracting Member States is an inherent consequence of bilateral double taxation conventions. It follows that a taxable person resident in Belgium is not in the same situation as a taxable person resident outside Belgium so far as concerns wealth tax on real property situated in the Netherlands.’<sup>553</sup>

Determining justification at the comparability level is also practiced by the European Court of Human Rights (ECHR) as will be seen in Chapter 5. This supports the

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<sup>550</sup>Case C-512/03, *J.E.J. Blanckaert v Inspecteur van de Belastingdienst/Particulieren/OndernemingenbuitenlandteHeerlen*, (2005) I 7685 para 51.

<sup>551</sup> *Truck Center Case* (n 492).

<sup>552</sup> Case C-376/03, *D. v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen* (2005) I 05821

<sup>553</sup> *Ibid.*, para 61.

relevance of this approach in discrimination cases. In some cases, it is more practical to determine the justification during the assessment of likeness. Although this approach would likely depart from the three-prong test as in *Pope & Talbot, Inc v Canada* (which is similar to GATT/WTO), it could be an effective method of interpretation.<sup>554</sup> Chapter 6 will elaborate on the suitability, practicality and application of the merged justification test in investment cases.

## **5.0 Justifications**

### **5.1 Common Justifications Brought by Member States**

Justifications for discriminatory measures can be brought under the exceptions provided for in the TFEU. A notable exception for free movement of capital contains in Articles 64 and 65 of the TFEU which provide for justifications on the application of third countries, public policy and public security. On a wider scope, and where there is no direct exception, the court also construes justifications by reasons of ‘overriding general interest’<sup>555</sup> coupled with the principle of proportionality in which makes any justification confined only to what is necessary to achieve the legitimate objectives.<sup>556</sup> This is also where the ‘rule of reason’ takes place.<sup>557</sup> It is observed that the ECJ has been very reluctant in accepting most of the justifications brought forth

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<sup>554</sup> In investment cases, the general approach taken by the tribunals are by considering three matters, firstly whether the comparators are in like situations, secondly, whether there is less favourable treatment and thirdly whether there is any reasonable justification for the discriminatory treatment. See *Pope & Talbot Inc v Canada* (Award on the Merits of Phase 2, 10 April 2001), para 78.

<sup>555</sup> Difference in treatment applies to situations which are not objectively comparable or is justified by overriding reasons in the general interest (Case C-35/98 *Verkooijen* [2000] ECR I-4071, para 43, and Manninen, (n 529), paras 28 and 29).

<sup>556</sup> See, to this effect, the judgments in *Futura*, (n 543), para 26; *Gebhard*, (n 499), para 37; Case C-19/ 92 *Kraus* [1993] ECR I-1663, para 32; and Case C-415/ 93 *Bosman* [1995] ECR I-4921, para 104.

<sup>557</sup> *Cassis de Dijon*, (n 35).

by the member states in defending their regulatory measures in both FoE and FMoC.<sup>558</sup> The reluctance is generally due to the difficulty in proving strong and convincing justifications by the member states against the clear and precise aim of the European Union to achieve an internal market.

a. Cohesiveness of National System/ Fiscal Supervision

The ECJ has accepted the justification on the ground of maintaining the cohesiveness of national tax system in the case of *Bachman*. This defence is popularly known as the ‘*Bachman* defence’ in EU literatures. In *Bachman*, the court stated:

‘...that the need to maintain the cohesion of the tax systems could, in certain circumstances, provide sufficient justification for maintaining rules restricting fundamental freedoms...’<sup>559</sup>

The court also mentioned in the case of *Manninen* that safeguarding the coherence of the tax system is compatible with the Treaty provisions but it must not go beyond what is necessary to attain the objective of the legislation.<sup>560</sup> This defence is however accepted by the court if there is a direct link of the discriminatory measure to the justification of cohesion of the national tax system. In the cases cited, there was a direct link between the deductibility of contributions from taxable income and the taxation of sums payable by insurers under old-age and life assurance policies, and that link had to be maintained in order to preserve the cohesion of the tax system in

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<sup>558</sup> Luca Cerioni, *EU Corporate Law And EU Company Tax Law* (Edward Elgar Publishing 2007) 38.

<sup>559</sup>Case C-204/90 *Bachmann* [1992]ECR I-249 and Case C-300/90 *Commission v Belgium* [1992] ECR I-305).

<sup>560</sup>*Manninen*, (n 529) para 29; *Verkooijen*, (n 555) para 43.

question. In the case of *Imperial Chemical Industries plc (ICI) and Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)*<sup>561</sup> however, as there was no such direct link between the consortium relief granted for losses incurred by a resident subsidiary and the taxation of profits made by non-resident subsidiaries, the ECJ precluded the member state's legislation brought under this justification. The Bachman case was rather an exception than a rule. In the case of *Bosal*, over taxation cannot be justified to preserve the coherence of the tax system.<sup>562</sup>

#### b. Avoidance of Taxation

The court accepts avoidance of taxation as a justification if it can be proven that there are wholly artificial arrangements to circumvent the national tax provisions. In the case of *Centros*, while precluding the measure of the state which refused to register a branch of a company formed in another member state that have no actual business in that state, the court did not reject the possibility of considering this justification in the event of fraud. The court held:

‘...That interpretation does not, however, prevent the authorities of the Member State concerned from adopting any appropriate measure for preventing or penalising fraud, either in relation to the company itself, if need be in cooperation with the Member State in which it was formed, or in relation to its members, where it has been established that they are in fact attempting, by means of the formation of a company, to evade their

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<sup>561</sup>Case C-264/96 ICI [1998] ECR I-0000, para 29.

<sup>562</sup>*Bosal*, (n 93), para 34. Other cases which rejected cohesiveness as a justification were C-80/94 *G.H.E.J Wielockx v Inspecteur der Directe Belastingen* [1998] ECR I-02493 paras 23-27 and *Schumacker*, (n 488).

obligations towards private or public creditors established in the territory of the Member State concerned.<sup>563</sup>

Another condition that the court requires before invoking avoidance of taxation as a justification is that it must already occurred. In *Lasteyrie*, a French legislation provided lesser treatment to taxpayers who intended to transfer their residence for tax purposes outside France as compared to those who retained in France. The court held that the taxation on ‘immediate taxation on increases in value’ on the first category of taxpayers was unjustified as they have not yet been realised ('latent increases in value').<sup>564</sup>

### c. Principle of Territoriality

In terms of territoriality, the court accepted and recognised that resident companies are of ‘unlimited taxation’ (taxed on their worldwide profits) while non –resident companies are of ‘limited taxation’ (taxed on profits from the source in the taxing state). In the case of *Marks & Spencer*, the court acknowledged this principle as accepted by the EU law:

‘In a situation such as that in the proceedings before the national court, it must be accepted that by taxing resident companies on their worldwide profits and non-resident companies solely on the profits from their activities in that State, the parent company's Member State is acting in accordance with

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<sup>563</sup> *Centros* (n 522).

<sup>564</sup> *Lasteyrie du Saillant*, (n 491), paras 63-69.

the principle of territoriality enshrined in international tax law and recognised by Community law.<sup>565</sup>

The court in the case of *Manninen* however did not extend justification under the ground of territoriality if the categories of dividends concerned by that difference in treatment share the same objective situation.<sup>566</sup>

#### d. Capacity of the State

The question which arose in the case of *Truck Center* was whether the retention of tax at source on interest paid by a company resident, which was in Belgium to a recipient company resident in another state, Luxembourg was discriminatory. The interest paid to a recipient company resident in the host state was however exempted from the retention. Despite the discriminatory surface of the treatment, the court accepted that the companies were objectively comparable. The reasoning was based on the different legal bases on which the legislation was based on. Among the justification was the capacity of the state in both circumstances. Belgium was in the capacity of State of residence when the company paying and receiving that interest is resident in Belgium, and holds the capacity of the State in which the interest originates when a company resident in Belgium pays interest to a non-resident company. When both the companies paying the interest and receiving that interest are resident in Belgium, the position of the Belgian State becomes different to (that

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<sup>565</sup>Case C-446/03 *Marks & Spencer plc v Halsey (Her Majesty's Inspector of Taxes)* [2005] ECR I-10837, para 39.

<sup>566</sup>*Manninen*, (n 529), para 39.

in which it finds itself) when a company resident in Belgium pays interest to a non-resident company. In the first case, the Belgian State acts in its capacity as the State of residence of the companies concerned, while, in the second case, it acts in its capacity as the State in which the interest originates. This is termed as the ‘source state capacity’ and the ‘residence state capacity’.<sup>567</sup>

e. Reduction in Tax Revenue

The EU law does not accept the reason of reduction in tax revenue as constituting overriding reasons in the public interest. In *Manninen* the court mentioned,

‘...it has been consistently held in the case-law that reduction in tax revenue cannot be regarded as an overriding reason in the public interest which may be relied on to justify a measure which is in principle contrary to a fundamental freedom.’<sup>568</sup>

The court upheld similar decisions in the case of *Verkooijen*, *Danner* and *X&Y*.<sup>569</sup>

f. Public Interest

The EU has provided exceptions for abolition of restrictions in the TFEU. As for public policy, the EU has adopted a strict guideline. In the case of *Eglise de*

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<sup>567</sup> *Truck Center Case*, (n 492), para 42. See also O’Shea, ‘Truck Center: A Lesson in Source vs. Residence Obligations in the EU’ (n 128); Werner, ‘Analysis of the ECJ’s Recent Judgment in Case C282/07, *Etat belge-SPF Finances v Truck Center*’ (n 524).

<sup>568</sup> *Manninen*, (n 529), para 49.

<sup>569</sup> *Verkooijen*, (n 555) para 59, Case C-136/00 *Danner* [2002] ECR I-8147, para 56 and Case C-436/00 *X and Y v Riksskatteverket*, 2002 I-10829, para 50.

*Scientologie*, the administrative declaration imposed by the French government, invoking ‘threat to public policy’ was held to be incompatible with the EC Treaty for the reason of its generality and resulting to less clarity to the persons concerned. The measure must be proven that it is taken only when the objective cannot be achieved by a less restrictive measure. The public policy justification must also be detailed and must not result to the law being less clear, which will then be against the ‘principle of legal certainty.’<sup>570</sup> A similar approach is adopted in the case of *Alfredo Albore* where the Italian law which imposed on nationals of other member states administrative authorisation for any purchase of real estate situated within an area of the national territory designated as being of military importance, was found incompatible with the EC Treaty. The court was not satisfied with the discriminatory measure introduced and insisted that it is necessary to show that ‘non-discriminatory treatment of the nationals of all the Member States would expose the military interests of the Member State concerned to real, specific and serious risks which could not be countered by less restrictive procedures.’<sup>571</sup>

g. Reciprocity

The court looked at this justification unfavourably in the case of *Avoir Fiscal*.<sup>572</sup> According to France, only countries having Double Taxation Conventions (DTCs) with France could enjoy the *Avoir fiscal*. This means, companies of other member states would receive differential treatment. Similarly, the ECJ rejected this

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<sup>570</sup>Case C-54/99 *Association Église de Scientologie de Paris, Scientology International Reserves Trust and The Prime Minister* [2002] ECR I-1335, para 22.

<sup>571</sup>Case C-423/98 *Alfredo Albore* [2000] ECR I-05965, para 24.

<sup>572</sup>*Avoir Fiscal Case*, (n 464), para 26.



justification in the case of *St. Gobain*, emphasizing that in entering into DTCs, the member states are still subjected to the parameters of the Community law.<sup>573</sup>

## **5.2 Analysis of the Justifications Brought by Member States**

### *5.2.1 The ECJ Strict Approach*

The justifications brought by the member states are mostly precluded despite the fact that some of them are accepted in principle.<sup>574</sup> The thresholds in accepting the justifications are high. The member states in the EU have given away a huge scope of power to the EU, effectively giving the EU law the right to interpret matters in its own perspective, even if it is contrary to the domestic interpretation. The domestic interpretation in such cases would not be upheld if the EU decides that its own interpretation is necessary for the furtherance of internal market.<sup>575</sup> It must be realised that the EU law carries at least three interests, the interest of the claimant, the member state that is challenged and the interest of the EU as a regional integration. In most of the decisions, the EU speaks for itself. This can be seen in the usage of certain phrases such as ‘less attractiveness’ or ‘compatibility’ which

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<sup>573</sup> *Saint-Gobain*, (n 546) paras 55-63.

<sup>574</sup> Justifications which are in principle accepted by the court are evasion of tax, avoidance of abuse and coherence of tax. See discussion in 5.1 and cases e.g. *Manninen* (n 529), *Centros* (n 522) and *Futura* (n 543).

<sup>575</sup> For instance, in the *Centros* case, Denmark contended that the determination of the registration of branch should be within the domestic perusal considering that there was no business held by the company at its incorporation place. However the ECJ ruled that the result of refusing registration of the branch which is otherwise allowed for non-nationals would lead to the denial of freedom of establishment. This indicates that the supremacy and the direct effect of the EU law in the member states’ legal system are the factors that differ to the international investment legal regime. See *Centros*, (n 522), para 16, 21.

indicate the furtherance of its own objectives.<sup>576</sup> This is why the principle of proportionality plays an important role in setting the right limits of the application of the freedoms or measures by the member states on the one hand and the EU on the other.<sup>577</sup>

The justifications brought by the EU member states – coherence of the national system, avoidance of double taxation *etc*, would perhaps make a better way in the investment tribunals. This is where the effect of the EU deeper integration marks the demarcation line with that of the investment regime. This could be seen from the ECJ decisions which are reluctant to accept justifications, or to accept with heavy restrictions in order to prioritise the achievement of the internal market. The investment treaties on the other hand are negotiated limited to the extent of

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<sup>576</sup> In view of satisfying the aim of internal market, the ECJ has in many occasions out ruled the justifications of the member states on the ground that the regulation or restriction would make it ‘less attractive’ for member states’ residents for establishment in another member state. While this may be a common remark made by the ECJ in assessing discrimination cases, it may not be suitable, fear of it being taken afar, in the context of investment treaties as restrictions may be justifiable even though they appear to cause less attractiveness in the enjoyment of investment treaties. The term ‘less attractiveness’ may be appropriate if the investment treaties have similar ‘notion of freedom’ as in the EU law. In the case of *Tankereederei*, the court held:

‘In the present case, it must be held that a national provision such as that at issue in the main proceedings – which applies a less favourable tax regime to investments used in the territory of other Member States, in which the undertaking concerned is not established, than to investments that are used in national territory – is likely, if not to discourage national undertakings from providing, in other Member States, services that require the use of capital goods situated in those other Member States, at least to make that provision of cross-border services less attractive or more difficult than the provision of services in national territory by means of capital goods situated in that territory’ (see, to that effect, *Jobra*, paragraph 24).

As in the EU law, even though a measure is not discriminatory, it is precluded nevertheless if it ‘hinders the exercise of the freedoms. While the EU law would conclude that there is a restriction on the freedoms whenever a national measure prohibit, impede or render less attractive the exercise of that freedom, the investment treaties confines itself (in the context of national treatment) only if the measure discriminates a foreign investor. Resorting to determine and depending solely whether a discriminatory measure would cause less attractiveness to the exercise of the benefits of the investment treaties would render excess of jurisdiction and unacceptable. See C-287/10 *Tankereederei I SA v Directeur de l’administration des contributions directes*, [2010] I-14233 para 19 and the use of ‘dissuaded’ in *Bosal* (n 93), para 27 . As for compatibility see Case C-446/03 *Marks & Spencer plc v Halsey (Her Majesty’s Inspector of Taxes)* [2005] ECR I-10837 paras 35 and 51, and *Manninen*, (n 529), paras 28, 29.

<sup>577</sup> An elaboration on the principle of proportionality in the EU law will be discussed in the subsequent section.

investment protection from state sovereignty. Acknowledging this, host states still possess a considerable level of regulatory power in exercising its sovereignty.

There are possibilities that justifications relating to cohesion of national tax system and national tax policy are brought in the investment cases. It is observed that all the justifications (in 5.1) brought by the member states have the potential to be accepted by the investment tribunals. The main reason is that the justifications as featured in EU cases are mostly involving sensitive domestic tax measures which override public interest. The lack of strong integration aim makes investment treaties not as encompassing as the EU law to overrule such measures. Nevertheless, they must be subjected to proportionality. In the case of *Feldman v Mexico*, there was in principle no objection on the justification of fiscal coherence but there must be reasonable nexus to the rational policy in which the host state intends to achieve.<sup>578</sup> In that case, the tribunal accepted that the refusal to grant rebate on the ground of, *inter alia*, ‘deprivation of government substantial amount of tax revenue’, was an objective and rational basis for treating producers and re-sellers differently.<sup>579</sup>

It is also pertinent to note that the ECJ has in particular expressed its rejection of any justification purely on economic reason. This is a general approach taken by the ECJ across the freedoms. If the measure is taken on purely economic grounds, it is not good enough to constitute a reason of public interest. In *Federación de disribuidores cinematográficos* the court held,

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<sup>578</sup> This test was developed in the case of *Pope & Talbot, Inc. v Canada*. See *Pope & Talbot, Inc. v Canada*, (n 20), para 78.

<sup>579</sup> This reason was brought along with other justifications. The justifications were to discourage smuggling, protect intellectual property rights and prohibit gray market sales. *Feldman v Mexico*, (n 15) paras 115 and 171.

‘16 ... It may also be seen from those judgments that objectives of an economic nature cannot constitute grounds of public policy within the meaning of that article.

17. There is no doubt that the Decree-Law pursues such an economic objective since by seeking to guarantee the distribution of a large number of national films it succeeds in ensuring sufficient receipts for the producers of such films.

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21. In those circumstances, the link between the grant of licences for dubbing films from third countries and the distribution of national films pursues an objective of a purely economic nature which does not constitute a ground of public policy within the meaning of Article 56 of the Treaty.’<sup>580</sup>

It remains unclear in the investment treaties in relation to transfer of fund whether the host states are allowed to introduce restrictive measures in situations of financial crisis. In the case of *CMS v Argentina* the tribunal held:

‘The third issue the Tribunal must determine is whether Article XI of the Treaty can be interpreted in such a way as to provide that it includes economic emergency as an essential security interest. While the text of the Article does not refer to economic crises or difficulties of that particular kind, as concluded above, there is nothing in the context of customary international

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<sup>580</sup>Case 17/92 *Federación de distribuidores cinematográficos* [1993] ECR I-2239. Among other purely economic grounds which were rejected by the court were considerations of a ‘national budgetary nature’. See Case C-109/04 *Kraneman* [2005] ECR I-2421 para 32.

law or the object and purpose of the Treaty that could on its own exclude major economic crises from the scope of Article XI.’<sup>581</sup>

The justification of economic crises may be acceptable in principle as in *Enron*<sup>582</sup> and *LG&E*<sup>583</sup> cases, but the tribunals differed on whether to approach the issue in a restrictive manner<sup>584</sup> and on the determination of the severity of an economic situation<sup>585</sup> entitled to justification.

It could be argued that since investment treaties are not as far reaching as the EU in the context of integration, the host states would have wider margin of appreciation in defending its national policies.<sup>586</sup> Some commentators put forth that investment treaties do have a role in answering to the call for ‘international cooperation for economic development’ in the ICSID preamble and similarly phrased objectives in many investment treaties<sup>587</sup> and highlight development as an ‘international right’ and

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<sup>581</sup>In the case of *CMS v Argentina*, a claim on discrimination was brought up alleging that ‘other public services relying on dollar –based tariff such as telephone companies, water distribution enterprises, banks, waterway transportation companies and other businesses, and significantly, the gas producers, have all been treated in a more favourable manner.’ The tribunal rejected the existence of discrimination as there was no intention to discriminate based on nationality and that similarity was not established either within the gas transportation and distribution industry or other utilities as well. The tribunal related it rather on the ground of fair and equitable treatment under the treaty. See *CMS Gas Transmission Company v. Argentine Republic*, ICSID case No. ARB/01/8, Award 12 May, 2005, para 293, 359.

<sup>582</sup>*Enron Corporation Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No ARB/01/3, Award, May 22, 2007.

<sup>583</sup>*LG&E Energy Corp., L&E Capital Corp., LG&E International Inc v. Argentine Republic*, ICSID case No. ARB/02/1, Decision on Liability, 3 October 2006.

<sup>584</sup>The tribunal in *Enron* applied restrictive interpretation. *Enron Case*, (n 582), para 331.

<sup>585</sup>*CMS v Argentina*, (n 581), para 355.

<sup>586</sup>A different viewpoint on this matter could be made in respect of more integrated investment treaties such as the ACIA and CAFTA-DR. This matter will be discussed in the subsequent paragraphs and partly in Ch.6.

<sup>587</sup>Omar E García-Bolívar, ‘Economic Development at the Core of the International Investment Law Regime’ (2010) <[http://works.bepress.com/cgi/viewcontent.cgi?article=1010&context=omar\\_garcia\\_bolivar](http://works.bepress.com/cgi/viewcontent.cgi?article=1010&context=omar_garcia_bolivar)>, accessed on 29 January 2014.

that there is a trend of new regional investment treaties and provisions going towards it.<sup>588</sup>

Generally, this issue may fall under deference given to host states. The investment tribunals have accorded deference in a number of cases, for instance *El-Paso v Argentina*, *Paushok v Mongolia* and *Feldman v Mexico*. In *El-Paso v Argentina*, the government accepted the host state's justification to balance for each sector the advantages and disadvantages of the general economic situation. This justification in effect allowed favourable treatment regarding the pesification measure to the banking sector which was locally run as compared to the oil and gas sector measure.<sup>589</sup> Similarly, in *Paushok v Mongolia* the tribunal accepted the justification of 'avoiding tax evasion in the gold mining industry' while in the case of *Feldman v Mexico* the tribunal accepted among others 'better control of tax revenues'.<sup>590</sup>

While wider scope of deference may suit well with general bilateral investment treaties, it may not be preferred in the interpretation of more integrated investment treaties. The ACIA and the AEC could, considering the wordings of the agreement, resort to the EU template of deciding cases. This means that deference will be reduced significantly as can be seen in EU cases. Similarly, in the context of CAFTA-DR and to some extent the NAFTA which are relatively more comprehensive trade and investment commercial network than general BITs, one could argue for narrower scope of deference.

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<sup>588</sup> Diane Alferez Desierto, 'Development as an International Right: Investment in the New Trade-Based IIAs' (2011) 3 Trade Law & Development 296.

<sup>589</sup> *El Paso v Argentina*, (n 173), para 310.

<sup>590</sup> *Feldman v Mexico*, (n 15), para 170; *Sergei Paushok, CJSC Golden East Company, CJSC Vostokneftegaz Company v The Government of Mongolia* UNCITRAL, Award on Jurisdiction and Liability, 28 April 2011, para 316. See elaboration of the cases in respect of deference in Ch.6 on Margin of Appreciation.

This first scenario would also lead to possible discontentment by member states, as to the intrusiveness of regulatory space. This could be seen in particular from the EU member states reactions on the ECJ recent rulings on direct taxation matters. The ECJ has portrayed a more expansive view of non-discrimination.<sup>591</sup> It would result to a back lash if the EU approach is adopted, it would render many national regulations violating the non-discrimination principle by restricting member states' flexibility over their own fiscal abilities.<sup>592</sup>

It is potential that the EU jurisprudence will be invoked in an ACIA case. It is anticipated that cases may arise under ACIA.<sup>593</sup> If the tribunals referred to the EU, there will obviously be more integration. The EU applies the *effet utile* principle to achieve the internal market and thus any form of discrimination may be barred. If this approach is preferred, the ECJ jurisprudence may be helpful.

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<sup>591</sup> Warren and Graetz, 'Income Tax Discrimination and the Political and Economic Integration of Europe' (n 521) 1194. On an interesting note, one would realise the different approach by the ECJ when commenting on justifications brought by third countries enjoying the FMOc. This follows the 'lack of aim' of internal market in the investment regime. See Hindelang, *The Free Movement of Capital and Foreign Direct Investment* (n 127) 24. This line of argument seemed to find consistency with some other passing commentaries on this *erga omnes* aspect of capital movement. In taxation matters and when touching on comparability of residents of the EU member states and third countries, it is repeatedly mentioned that they are not comparable due to the non-existence of tax treaties and thus entails justifications for difference of treatment. This indicates that though free movement of capital is granted, the third countries capital may face restrictions or discriminations due to this incomparability. Reflecting this to investment treaties, which has a lesser level of integration than the EU law, it is thought that perhaps the ECJ would also construe comparability test in a more strict manner as compared to if the case was adjudicated between residents of member states. Hence, in construing the judgments of the ECJ this research is cautious in excerpting lessons bearing in mind the aim of internal market as the fundamental philosophy of each ECJ decisions.

<sup>592</sup> Warren and Graetz, 'Income Tax Discrimination and the Political and Economic Integration of Europe' (n 521) 1253.

<sup>593</sup> The trend can be seen from other regional investor-state disputes such as NAFTA and CAFTA. Since the inception of NAFTA in 1994, there are 42 cases (up to 2005). See 'NAFTA Chapter 11 Investor-State Cases: Lessons for the Central America Free Trade Agreement' [2005] Public Citizen Global Trade Watch 11 <[http://www.citizen.org/documents/NAFTAREport\\_Final.pdf](http://www.citizen.org/documents/NAFTAREport_Final.pdf)> accessed 20 September 2013, < [http://www.citizen.org/documents/NAFTAREport\\_Final.pdf](http://www.citizen.org/documents/NAFTAREport_Final.pdf)>, accessed 20 September 2013. As for CAFTA, there at least six cases filed according to the U.S Department of State Diplomacy in Action website. See CAFTA-DR Investor State Arbitrations, < <http://www.state.gov/s/l/c33165.htm>>, accessed 20 September 2013.

However, this thesis takes the view that a holistic appreciation on the ASEAN political economy should be considered in determining the direction of interpretation in investment arbitrations. Learning from the impact of EU strict approach in interpreting discrimination cases, it is proposed that the ACIA adopts the general BIT approach. The *effet utile* principle can still benefit the investment regime if it is placed in the investment law perspective. Rather than eliminating all forms of restriction and discrimination, it is suggested that the national treatment provision under the purview of investment regime, only strikes down where purpose is apparently discriminatory. This seems to be the most appropriate approach which could reasonably be applied in the ACIA. It must be noted that ASEAN consists of member states with different economic positions. In the interpretation of justification for discrimination, this different level of development must be taken into account. This is an integral aspect of circumstances which could affect the ‘like circumstances’ assessment. The recognition of this difference is manifested in the ACIA in the guiding principles in Article 2. The article states that the liberal, facilitative, transparent and competitive investment environment in ASEAN must adhere to certain principles, *inter alia*, to grant special and differential treatment and other flexibilities to Member States depending on their level of development and sectorial sensitivities.<sup>594</sup> This reason, along with the differences in the legal systems, political ideology and the lack of support by institutions such the European Court of

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<sup>594</sup> Similar exemption is provided in Article 79 of the AEC that member states must provide special treatment to the least developed countries. See also discussions on the differences of the member states in both economic and non-economic positions that would impede integration. Muna Ndulo, ‘Harmonisation of Trade Laws in the African Economic Community’ (1993) 42 *International & Comparative Law Quarterly*; Theophilus Fuseini Maranga, ‘Colonial Legacy and the African Common Market: Problems and Challenges Facing the African Economic Community, The’ (1993) 10 *Harvard Blackletter Journal* 105; Gino J Naldi and Konstantinos D Magliveras, ‘African Economic Community: Emancipation for African States or Yet Another Glorious Failure, The’ (1998) 24 *North Carolina Journal of International Law and Commercial Regulation* 602.



Justice, the European Commission and the European Parliament, are said to be the challenges faced by the ACIA towards a full-fledged economic community.<sup>595</sup> In fact, it could be argued that the lack of such harmonisation institutions in the ACIA area is evidence of the member states' unwillingness to integrate closer along the line of the EU.

### *5.2.2 Proportionality*

The principle of proportionality prominently takes place in the ECJ decisions of freedom of establishment and free movement of capital. Its role is eminent to resolve the straddling of interests of the member states especially in the matter of direct taxation in FoE and FMoC against the interest of the EU which aims at ensuring the direct and full effect of the freedoms.<sup>596</sup>

The principle of proportionality works both sides, not only does it ensure that the restriction was necessary for achieving the aim of the EU law, it also ensures that any derogation must remain within the limits of the legitimate objectives in which it intends to pursue.<sup>597</sup> The first aspect of proportionality is by measuring the

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<sup>595</sup> To the contrary the AEC provides for the establishment of Court of Justice in Article 19 of the AEC. However, the challenges to it are obvious, due to the difference of legal systems, language, financing and independence of the system. Ndulo, 'Harmonisation of Trade Laws in the African Economic Community' (n 594). Some literatures also share the same view in respect of ACIA's slow progress towards achieving an economic union, see Tan, 'Will ASEAN Economic Integration Progress Beyond a Free Trade Area?' (n 516); Lin Chun Hung, 'ASEAN Charter: Deeper Regional Integration Under International Law?' (2010) 9 Chinese Journal of International Law 821.

<sup>596</sup> Direct taxation may constitute an obstacle to the EU by interfering with the efficient allocation of capital or incurrance of burden to residents of member states wanting to benefit from the freedoms. See Arginelli, 'The Discriminatory Taxation of Permanent Establishments by the Host State in the European Union: a Too Much Separate Entity Approach' (n 465) 86.

<sup>597</sup> Case C-423/98 Alfredo Albore, [2000] ECR I-05965 para 19. See also Case 222/84 *Johnston v Chief Constable of the Royal Ulster Constabulary* [1986] ECR 1651, paragraph 38

proportionality of the member states measure so that it does not exceed its legitimate objective. In *Gebhard*, the court emphasised:

‘...national measures liable to hinder or make less attractive the exercise of fundamental freedoms guaranteed by the Treaty must fulfil four conditions: they must be applied in a non-discriminatory manner; they must be justified by imperative requirements in the general interest; they must be suitable for securing the attainment of the objective which they pursue; and they must not go beyond what is necessary in order to attain it.’<sup>598</sup>

The EU law took into consideration the proper practice given in a particular matter in determining the justifiability of a discriminatory treatment.<sup>599</sup> In tax matters, the court similarly took the effort to understand/deliberate on the philosophy and technicalities of the effect of such tax measures, for instance by balancing the cohesion of tax system and the discriminatory and restrictive impact it would cause to nationals of another member state. In *Costa and Cifone*, the protection of public authorities against possible non-performance by the concession holder, in the light of the high overall value of the contracts which have been awarded to it was considered as disproportionate and therefore unjustified restrictions on the freedoms laid down

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<sup>598</sup> *Gebhard*, (n 499), para 37. See also Case C- 19/92 *Kraus v Land Baden-Württemberg* [1993] ECR I - 1663, para 32 and Case C-415/ 93 *Bosman* [1995] ECR I-4921, para 104, Case C-100/01 *Oteiza Olazabal* [2002] ECR I-10981, paragraph 43; Case C-527/06 *Renneberg* [2008] ECR I-7735, paragraph 81; Joined Cases C-155/08 and C-157/08 *X and Passenheim-van Schoot* [2009] ECR I-0000, paragraph 47; and Case C-169/08 *Presidente del Consigliodei Ministri* [2009] ECR I-0000, paragraph 42.

<sup>599</sup> An example of this is ‘proper practice in a given profession’ See Case C-96/85 *Commission v France* [1986] ECR 1485.

in Articles 43 EC and 49 EC.<sup>600</sup> In addition, if there is any less restrictive method to achieve a legitimate objective, the court may render a measure disproportionate.<sup>601</sup>

As for the other aspect of proportionality, it relates to the EU competency. In Article 5 (4) TEU (ex Article 5 TEC), this function of the principle of proportionality is made clear:

‘Under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties.’

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This provision disallows the interpretation of the ECJ that would overly emphasise on the aim of internal market when it was not necessary. For instance, if a measure is already in compliance with the EU law, it is not necessary to impose further requirements. In relation to this, the principle of proportionality controls the *bona fide* application of the freedoms. In *Centros*, the court held that if there is attempt to apply freedom of establishment by illicit arrangements or fraud ‘on the basis of objective evidence’ and to the disadvantage of the member state, the court may deny the freedom.<sup>603</sup>

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<sup>600</sup> Joined Cases C-72/10 and C-77/10 *Marcello Costa and Ugo Cifone* [2012] (*Costa and Cifone*), para 40.

<sup>601</sup> *Futura*, (n 543), paras 36-43.

<sup>602</sup> Consolidated Version of the Treaty of European Union, signed 7 February 1992, Official Journal of the European Union C115/13 of 9.5.2008, < <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:115:0013:0045:EN:PDF>>, accessed 21 September 2013.

<sup>603</sup> A mere option of a national to choose the least restrictive jurisdiction to set up a company or to perform business does not amount to fraud, but inherent in the exercise of the freedoms in a single market. See *Centros*, (n 522), paras 25, 27.

Proportionality is normally perused in the context of the legitimacy of the national measures in investment cases. Less is noticed on the second aspect of proportionality – on whether the interpretations proposed by the claimants or decided by the tribunals in its *ratio decidendi* are actually within the proportionate competence of an investment treaty or have actually exceed it. By highlighting the principle of proportionality in both of these aspects in investment arbitration, it could lead to a balanced interpretation of national treatment acceptable to both foreign investors and host states.

## **7.0 Conclusion**

There are two major points that investment law could learn from the ECJ. Firstly is on how the ECJ focuses on the situations of comparators in its likeness analysis (see 4.1) and secondly is by the application of the *effet-utile* principle. These two elements provide helpful insights to develop the interpretation of national treatment in investment treaties. They revive the meaning of ‘circumstances’ or ‘situations’ in the assessment of likeness and directs the interpretation towards achieving the functions of national treatment in the context of investment treaties. The EU cases have also shown how analysing likeness is possible and practical without restricting to the three-prong method by examining justification at the comparability stage. This feature is similar to the observation on the International Human Rights jurisprudence, in particular the ECHR cases. As will be explained in Chapters 5 and 6, there would be instances that the tribunal should adopt this approach. As discussed in this chapter, the EU law could potentially be referred to by the new emerging free trade and investment agreements which provide for pre-establishment rights such as

the ASEAN Comprehensive Investment Agreement 2009, AEC and the CAFTA-DR. It is unable to predict the direction of these treaties due to the limited number of cases. In this regard, this thesis suggests that the arbitrators should take cognisance of the importance of deference that is more apparent in the investment tribunals and the differences in the level of development of member states as enshrined in the treaties. This is also a lesson learnt from the EU interpretations which has reflected the furtherance of the EU aims and objectives, while rendering less regard on the member states' interests. It is submitted that a balanced approach is needed that could cater both the member states' and foreign investors/investments' interest for the effectiveness and sustainability of international investment law.

## Chapter 5

# RELEVANCE OF INTERNATIONAL HUMAN RIGHTS LAW (IHR) ON PROPERTY TO NATIONAL TREATMENT IN INTERNATIONAL INVESTMENT LAW

## 1.0 Introduction

The interaction between international human rights law and international investment law has generally been on several grounds. Among those which are discussed and adjudicated are the competing objectives of the jurisprudences, the substantive balancing of investors and human rights, the extent of a state's adherence to other international obligations<sup>604</sup> and the shared general principles that could benefit interpretation. This chapter aims at expanding the last aspect mentioned, i.e the relevance of the methodology of interpretation in discrimination cases.<sup>605</sup> The aim is

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<sup>604</sup> Conflicts often arise when public services are privatised and was later interfered by government measures (such as freezing water prices) leaving the investors facing human rights issues. A conflict between the objectives of the BIT and human rights can be seen in the case of *Azurix v Argentina*. It was contended that the the government's action was for the consumers' public interest on water as an essential human right. See *Azurix Corp v Argentine Republic* ICSID Case No ARB/01/12, Final Award, 14 July 2006, para 254. Other cases of this nature are *Suez, Sociedad General de Aguas de Barcelona SA and Interagua Servicios Integrales de Agua SA v The Argentine Republic* ICSID Case No ARB/03/17, Decision on Jurisdiction, 16 May 2006; *Aguas del Tunari SA v Republic of Bolivia* ICSID Case No ARB/02/3, Decision on Respondent's Objection to Jurisdiction, 21 October 2005'; *SAUR International v. Argentine Republic* (ICSID Case No. ARB/04/4). See also various scholarly articles and commentaries on this interaction in Pierre-Marie Dupuy, Francesco Francioni and Ernst-Ulrich Petersmann (eds), *Human Rights in International Investment Law and Arbitration* (Oxford University Press 2009).

<sup>605</sup> This kind of interaction would to some correspond to the harmonisation of the two regimes. See Bruno Simma and Theodore Kill, 'Harmonizing Investment Protection and International Human Rights: First Steps Towards a Methodology' in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP Oxford 2009); A Dias, 'Investing in Human Rights Protection - The Soundest Investment of All?' (2013) 10 Transnational Dispute Management (TDM) <<http://www.transnational-dispute-management.com/article.asp?key=1934>>, accessed on 24 January 2013.; Ursula Kriebaum and Christoph Schreuer, 'The Concept of Property in Human Rights Law and International Investment Law' in Stephan Breitenmoser, Bernhard Ehrenzeller and Marco Sassoli (eds), *Human Rights*,

to compare the judicial approaches taken by the European Court of Human Rights (ECtHR or hereinafter ‘the Court’) and to benefit them to the extent suitable to international investment law in the interpretation of the non-discrimination principle. This subject has received less attention in the light of comparison in the two jurisprudences albeit its potentials.<sup>606</sup> The motivation for this exercise is the quest to search for guidance in the interpretation of national treatment in investment treaties.

Protection of property as a component of international human rights is covered under various conventions. Article 17 of the Universal Declaration of Human Rights (UDHR) stipulates that everyone has the right to own property and shall not be arbitrarily deprived of it.<sup>607</sup> Among the main human rights instruments which embody the right to property are the European Convention of Human Rights (ECHR),<sup>608</sup> the American Convention of Human Rights (ACHR),<sup>609</sup> the Protocol to the African Charter on the African Court on Human and Peoples’ Rights (ACHPR),<sup>610</sup> the United Nations Covenants on Economic, Social and Cultural

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*Democracy and the Rule of Law: Liber Amicorum Luzius Wildhaber* (Mul, Nomos Verlagsgesellschaft 2007); Pierre-Marie Dupuy and others (eds), ‘Unification Rather Than Fragmentation of International Law? The Case of International Investment Law and Human Rights Law’, *Human Rights in International Investment Law and Arbitration* (Oxford University Press 2009).

<sup>606</sup> For instance, in a recent article there seem to be a wide coverage on areas of convergence of international human rights and investment treaties including expropriation, full protection and security and fair and equitable treatment but did not include non-discrimination except in brief with the discussion of NAFTA and indigenous discrimination. See TG Nelson, ‘Human Rights Law and BIT Protection: Areas of Convergence’ (2013) 10 Transnational Dispute Management (TDM) <<http://www.transnational-dispute-management.com/article.asp?key=1936>>, accessed on 24 January 2013. A notable exception is an article by Freya Baetens, see Freya Baetens, ‘Discrimination on the Basis of Nationality: Determining Likeness in Human Rights and Investment Law’ (n 97).

<sup>607</sup> This right maintains as a general recognition until when it was later included in other human rights instruments which have binding effect.

<sup>608</sup> Convention for the Protection of Human Rights and Fundamental Freedoms, adopted 4 November 1959, entered into force 3 September 1953

<sup>609</sup> Article 21 (2) ACHR contains rights to property.

<sup>610</sup> The right of property is contained in Article 14 ACHPR.

Rights<sup>611</sup> and on Civil and Political Rights<sup>612</sup> and Fundamental Rights Charter (FRC).<sup>613</sup>

The international human rights jurisprudence, similar to international investment law also holds the non-discrimination principle as an important element of the treaties. Equally, it also protects the right to property. These are the main commonalities between the two jurisprudences that lead to this study.

The major focus of this chapter is the ECHR, in particular Article 1 Protocol 1 (A1P1) on the right to property taken together with Article 14 which prohibits discrimination. Other applications of Article 14 ECHR will however be construed when necessary, especially the cases that contain important decisions or guidelines which are applied across the various rights.<sup>614</sup>

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<sup>611</sup> Article 2 ICESCR.

<sup>612</sup> Article 3 ICCPR. The ICCPR does not incorporate protection to property as a fundamental right but incorporates it with the prohibition of discrimination in Article 3. Although it is an important international human right instrument at the universal level it, if one is to talk about expropriation, it has ‘weak foundation’ for such investment protection. See Christian Tomuschat, ‘The European Court of Human Rights and Investment Protection’ in Christina Binder and others (eds), *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP Oxford 2009) 638.

<sup>613</sup> Article 21(1) FRC provides ‘Any discrimination based on any ground such as sex, race, colour, ethnic or social origin, genetic features, language, religion or belief, political or any other opinion, membership of a national minority, property, birth, disability, age or sexual orientation shall be prohibited.’ By the accession of European Union to European Convention for the Protection of Human Rights and Fundamental Freedoms, the EU is obliged to respect the fundamental rights contained in the convention. These rights are incorporated in the Charter of Fundamental Rights of the European Union (2000/C 364/01). See also Article 6(2) of the Treaty of Lisbon on the accession of the EU.

<sup>614</sup> It is pertinent to note that the Article 14 is dependant and must be accompanied by a substantive claim. Thus, it could be invoked with other various rights in the ECHR, to name a few A1P1, Article 6, Article 8 and Article 9. The general principles employed in the interpretation of the non-discrimination principle across other jurisprudences could arguably be instructive as there is no indication that there should be any difference in determining likeness in relation to property or nationality namely the search for analogous situations, objectivity and reasonableness of the measure and the reasonable relationship of proportionality between the means employed and the aim sought to be realised. See Freya Baetens, ‘Discrimination on the Basis of Nationality: Determining Likeness in Human Rights and Investment Law’ (n 97); *Thlimmenos v Greece* (Application No. 34369/97) Decided on Merits, 6 April 2000; *Case “Relating to Certain Aspects of the Laws on the Use of Languages in Education in Belgium v. Belgium* (Merits)(Application No 1474/62; 1677/62; 1691/62; 1769/63; 1994/63; 2126/64). Article 14 accompanied with Article 1 Protocol 1 are the closest match



This chapter is aimed at examining how a discrimination case is construed in the ECHR and other instruments of international human rights especially in the determination of likeness or similarity of the comparators. The question related to this exercise is to find out whether there are characteristics or concepts applied in determining the proper comparator which could be benefitted by international investment law. This chapter will reveal that while there are a few noticeable traits in the determination of likeness, there are concepts that have even played a major role, namely the concept of margin of appreciation and proportionality which are applied by the court. The application of margin of appreciation and proportionality would create the legitimate expectation for states and private parties on how likeness is construed in discrimination cases.

Comparison is made not without caution. The relevance of the characteristics or concepts will be discussed in the light of compatibility and appropriateness of the philosophy which will be perused in the subsequent section and will be re-emphasised after the characteristics and concepts are put forth.

## **2.0 Reasons for Reference to the ECHR**

It is observed that there is an emerging trend of reference to the ECHR jurisprudence in international investment arbitrations. This attempt has been highlighted in several

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to the national treatment provision in investment treaties. Cases which brought claims under these articles have questioned the legitimacy of discriminatory measures by member states which have allegedly infringed the enjoyment of property by individuals. This may also include investors. This will be explained in the subsequent subsection.

cases<sup>615</sup> and scholarly writings,<sup>616</sup> but not as yet advanced in the context of national treatment. On the surface, this may be primarily due to the non-existence of a direct reflection of the national treatment provision as one may find in Article III of GATT/WTO. The non-existence of such direct reflection should not however deter reference to international human rights law. The ECHR in its jurisprudence of non-discrimination contained in Article 14, coupled with the protection of property in AIP1 provides similar concerns for adjudication, asks the same questions (i.e the search of comparator, discriminatory treatment and the rationale of the measure) and provide structurally similar opportunities for individuals (or investors) to bring direct claims against states' alleged discriminatory measures in front of the ECtHR.<sup>617</sup> Especially in respect of AIP1, it is increasingly being invoked by businesses, including investments to challenge regulatory measures which interfere with the enjoyment of their possessions.<sup>618</sup> Such regulatory measures may give rise to actions both under investment treaties as expropriation claims or human rights instruments.<sup>619</sup> Observed further, when AIP1 is taken together with Article 14

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<sup>615</sup> See for example cases which referred to the ECHR jurisprudence, for instance the cases of *Mondev* and *Tecmed* in determining civil rights in the interpretation of Article 6 (1) of the European Convention and the issue of proportionality. *Mondev International Ltd v US*, (n 64); *Tecnicas Medioambientales TECMED S.A. v. The United Mexican States* ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003. See also relevant articles such as Elyse M Freeman, 'Regulatory Expropriation Under NAFTA Chapter 11: Some Lessons from the European Court of Human Rights' (2003) 42 Columbia Journal of Transnational Law 177.

<sup>616</sup> See list of reference on this matter at (n 605) above.

<sup>617</sup> The structurally similar characteristics of individual-state claim create a basis of analogy. The same view is made in the context of TRIPS. See Laurence R Helfer, 'Adjudicating Copyright Claims Under the TRIPS Agreement: The Case for a European Human Rights Analogy' (1998) 39 Harvard International Law Journal 357.; Tomuschat, 'The European Court of Human Rights and Investment Protection' (n 612) 636.

<sup>618</sup> The provision has been taken as a 'commercial character and been used extensively by business in the advancement of its interests'. See Robin CA White and Clare Ovey, *The European Convention on Human Rights* (5th edn, OUP Oxford 2010) 477. Examples of cases brought by companies are, *inter alia* *Segame SA v. France* – (App. 4837/06), 7 June 2012, ECHR 2012 -V; *Buffalo SRL in Liquidation v. Italy*, (App. 38746/97), 3 July 2003, ECHR 2033-1; *Eko-Elda AVEE v Greece*, (App. 10162/02), 9 March 2006, ECHR 2006-IV; see also Marius Emberland, *The Human Rights of Companies: Exploring the Structure of ECHR Protection* (OUP Oxford 2006).; Tomuschat, 'The European Court of Human Rights and Investment Protection' (n 612) 642.

<sup>619</sup> A similar measure or government policy has even given rise to possible claims under both investment treaties and international human rights instruments. For instance, the Zimbabwe land

ECHR which prohibits non-discrimination, it could result to the same effect as a national treatment provision in international investment law when it is invoked against a better treatment given to nationals of the host state.<sup>620</sup>

Secondly, it is due to the immaturity of international investment regime relative to international human rights.<sup>621</sup> The whole exercise is not to undermine the potential of international investment law to develop its own interpretation. It is submitted that while the interpretation in accordance to the ordinary meaning of the terms in their context and in the light of the object and purpose of the treaties is a mandatory obligation that precedes other methods of interpretations,<sup>622</sup> the minimalist nature of investment treaty provisions leaves the international investment tribunals in inadequate guidance.<sup>623</sup> In the context of national treatment for instance, interpreting the ordinary meaning of the words ‘in like situation’ or in ‘like circumstances’ may end up meaningless as they are relative in nature, which rather needs the way to

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reform led to a case under ICSID and a case under SADC, invoking human rights protection. See *Bernardus Henricus Funnekotter and Others v. Republic of Zimbabwe*, ICSID Case No. ARB/05/6, Award, 22 April 2009 and *Mike Campbell (Pvt) Ltd and Others v. Republic of Zimbabwe*, SADC Case No. 2/2007 (Nov. 28, 2008). See also Gino J Naldi, ‘Mike Campbell (Pvt) Ltd et Al v The Republic of Zimbabwe: Zimbabwe’s Land Reform Programme Held in Breach of the SADC Treaty’ (2009) 53 *Journal of African Law* 305; Ben Love, ‘Introductory Note to the International Centre for Settlement of Investment Disputes: *Funnekotter and Others v Republic of Zimbabwe*’ (2009) 48 *International Legal Materials* 760.

<sup>620</sup> In the case of *Darby v Sweden*, the differential treatment between resident taxpayers and non-resident taxpayers in the right to opt out of paying church tax violated Article 14 taken together with A1P1. See *Darby v Sweden*, (App.11581/85), 23 October 1990, Series A, No 187, (1991) 13 EHRR 774.

<sup>621</sup> Roberts, ‘Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System’ (n 322); Walde, ‘Comments on the Discipline of National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?’ (n 3); Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’ (n 102).

<sup>622</sup> Articles 31, 32 and 33 of the Vienna Convention of the Law of Treaties provide the method of interpretation of international treaty which is also a reflection of customary international law. See *Anena (Mexico v United States)* 2004 ICJ, 37-28/83, *Sovereignty over Pulau Ligitan and Pulau Sipadan (Indonesia v. Malaysia)*, Judgment, 2002 I.C.J. 645 (Dec. 17). The application of these treaty interpretation articles in investment arbitrations is capable of not only interpreting the treaties in line with the customary international notions, but can be used to ‘fill the open-ended language’ by way of, inter alia reference to the ECHR jurisprudence. Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ (n 539) 732.

<sup>623</sup> Roberts, ‘Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System’ (n 322).

construe likeness more than its literal meaning. Thus the tools needed in construing likeness are vital in this process. The vague provisions of national treatment in investment treaties need to be elaborated, and an effective and plausible way of achieving this is by referring to the established practice of other jurisprudences which address similar concerns. This could be learnt not only from the relevant investment treaty, but other investment treaties<sup>624</sup> and even from other jurisprudence having analogous protection by way of adverse or negative interpretation.<sup>625</sup> Tendency would be to seek similar interpretations elsewhere in the international legal fraternity especially where it is well practised and established.<sup>626</sup> It is observed that to the extent that an interpretation serves similar purpose and useful in the understanding of a concept, there is no reason that the interpretation in international investment law must be different merely because it belongs to another legal discipline. The equitable result may be the same.<sup>627</sup> Thus analogous interpretations in other jurisprudence can be useful as an ‘interpretative aid’, ‘instructive’ or ‘supplemental guidance’ in forming the context of national treatment or how to construe a case of discrimination.<sup>628</sup> Both ways, it is still in line with the VCLT

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<sup>624</sup> This is to acknowledge that since the investment treaties are not one and the same, they are strikingly similar to each other (except with small linguistic differences), so much that they form a regime as a result of cross-reference. See Schill, ‘Multilateralization through Interpretation: Producing and Reproducing Coherence in Investment Jurisprudence’ (n 496).

<sup>625</sup> Gerald Fitzmaurice in the oral proceedings relating to Reparation for Injuries Suffered in the Service of the United Nations mentioned this negative interpretation as a useful methodology in interpretation, ‘It often happens that when a problem is difficult or novel, as I think the present one is, the best method of approach to it is the negative rather than the positive one. In order to ascertain what a thing is, it is sometimes very useful to begin by enquiring what it is not, and in order to decide what exactly is covered or involved by a certain question, it may be well to determine first what is not involved by that question.’ See Reparation for Injuries Suffered in the Service of the United Nations, Pleadings, ICJ, 9<sup>th</sup> March 1949, p.111.

<sup>626</sup> Anthea Roberts, ‘Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System’ (n 322).

<sup>627</sup> Freeman, ‘Regulatory Expropriation under NAFTA Chapter 11’ (n 615).

<sup>628</sup> The terms ‘interpretative aid’, ‘instructive’, and ‘supplemental guidance’ has been used by Prof. David D. Caron concerning the interpretation of Article 11 (7) and (2) of the US-Ecuador BIT and analogous arbitral and scholarly interpretation of analogous language in other arbitral tribunals (for instance the US Model BIT, Article 10(2) of the ECT, the ECHR and ICJ. See *Chevron Corporation and Texaco Petroleum Company v Republic of Ecuador*, UNCITRAL/ PCA Case No.2009-23, Expert Opinion of Prof. David.D. Caron as to Art. 11(7) of the Treaty, 3 September 2010, <

Article 31-33, that in the quest of interpretation it must be done according to its text and context, and that a comparative exercise could help in achieving it.

Thirdly, the principles applied in the human rights jurisprudence can be regarded as general principles of international law. The development of jurisprudence in human rights instruments, in particular the ECHR has been influenced by the interaction and adoption of the common general principles or constitutional norms of national European legal orders.<sup>629</sup> In this regard, the principles of non-discrimination and property rights are to a large extent common to both international human rights law and international investment treaties and thus, arguably could be considered as general principles of law under article 38 of the ICJ Statute. Following this line of argument, the international human rights jurisprudence becomes a relevant source of law in which investment arbitrations should take cognisance of.<sup>630</sup> On a micro level observation of the construction of the non-discrimination principle in the international human rights law, the court applies similar tests in particular the search of analogous situations and the legitimacy of the aim pursued. These are potential aspects in which investment arbitration could learn from.

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<http://www.italaw.com/sites/default/files/case-documents/ita0241.pdf> >, accessed on 10 October 2013, paras 60, 80 and 138.

<sup>629</sup> The European legal orders include civil and common law legal systems, in particular of that of UK and France which has influenced other jurisdictions all over the world as a result of past colonisation.

<sup>630</sup> Walde has also emphasised the use of general principle of law under article 38 (1) (c) of the ICJ Statute to extend the application of comparative administrative law principles such as deference (margin of appreciation) and proportionality. This chapter is also responding and addressing Walde's concern of this underdeveloped area by highlighting the principles of margin of appreciation and proportionality in the interpretation of national treatment as will be explained in the subsequent sections. Walde, 'Interpreting Investment Treaties: Experiences and Examples' (n 539) 734.

### 3.0 Underlying Philosophies

The commonality of the underlying philosophies of international human rights and investment treaties forms part of the reason for this comparison. The protection and promotion of investments in investment treaties can be regarded as the ‘human rights’ (so as to use the term loosely) of foreign investors.<sup>631</sup> In a similar vein, certain protections in the international human rights instruments such as the right to property and the principle of non-discrimination can appear as human rights of companies which may be owned by foreign investors.<sup>632</sup>

Thus the two jurisprudences can be seen as complementing each other and to a large extent similar. By promoting the foreign investors’ rights, it is actually also promoting human rights. On a practical note, the same discrimination could give rise to claims under human rights law and investments. For instance, if Czech Republic issues a discriminatory measure that affects the enjoyment of property of say, a Dutch investor, the Dutch investor could bring a claim under the ECHR or alternatively under the Netherlands-Czech Republic investment treaty. An actual example is as in the Zimbabwe land reform measure that led to a case under ICSID and a case under SADC, invoking human rights protection.<sup>633</sup>

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<sup>631</sup> The rights are accrued to the investors or shareholders of investments. The term human rights may not be the appropriate term to refer to the rights contained in investment treaties due to the fundamental nature of human rights as inherent to human beings. Nevertheless, the ECHR despite being an instrument of international human rights explicitly extend the application of Article 1 Protocol 1 to natural and legal persons, which includes non-profitable or corporate entities. See also Charles Brower, ‘Corporations as Plaintiffs Under International Law: Three Narratives About Investment Treaties’ (2011) 9 Santa Clara Journal of International Law 179; Jose E Alvarez, ‘Critical Theory and the North American Free Trade Agreement’s Chapter Eleven’ (1996) 28 University of Miami Inter-American Law Review 303.

<sup>632</sup> Emberland, *The Human Rights of Companies* (n 618).

<sup>633</sup> See *Bernardus Henricus Funnekotter and Others v. Zimbabwe*, (n 619) and *Mike Campbell (Pvt) Ltd and Others v. Zimbabwe*, (n 619).

While the underlying philosophy of granting national treatment provision and non-discrimination principle in the GATT/WTO and EU are to facilitate liberalisation and to achieve an internal market respectively,<sup>634</sup> the international human right's underpinning philosophy is on the basis of fundamental human rights. The ECHR provides clearly in its preamble that it aims at 'securing the universal and effective recognition and observance' of the rights in the treaty for the 'further realisation of human rights and fundamental freedoms'.<sup>635</sup> The philosophy of the ECHR could be further understood from the history in which it was originated. The European states came into collaboration to ensure that European individual's rights are protected against the backdrop of the atrocities of World War II and the ideologies prevalent at that time i.e, fascism, communism and totalitarianism.<sup>636</sup> Fear of going back to the violations of human rights as occurred in the past, the ECHR aims at granting the essential civil and political rights which was then extended to property rights. The ECHR's main objective is the protection of human rights and fundamental freedoms including right to property contained therein.<sup>637</sup>

Similarly, the history of investment treaties would reveal the fragility of aliens' position in customary international law which led to the insertion of various substantive protections in the investment treaties.<sup>638</sup> The main motivation of the investment treaties is to protect investors or investment of nationals of the signing parties against unilateral takings and unfair treatment. This led to the signing of

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<sup>634</sup> Please refer to explanations of the underlying philosophy of GATT/WTO and the EU law in Ch.3 and 4 respectively.

<sup>635</sup> Preamble, ECHR. Similarly in the ICCPR preamble it emphasizes the respect and the observation of human rights.

<sup>636</sup> White and Ovey, *The European Convention on Human Rights* (n 618) 5.

<sup>637</sup> Emberland, *The Human Rights of Companies* (n 618) 160.

<sup>638</sup> Details on the position of the aliens in customary international law is explained in Ch.2.

bilateral treaties of friendship, commerce and navigation (FCN) in the 1820s and the conclusion of various investment treaties after World War II.<sup>639</sup>

The underpinning philosophy to protect human rights, fulfilled by the enjoyment of possession and non-discrimination in A1P1 and A14 is reflected in the assessment of discrimination to property in the ECHR. The ECHR contained right to property in Article 1 Protocol 1 which reads:

‘Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.’<sup>640</sup>

Similarly, the wording of Article 14 of the ECHR also suggests the protections covered in the convention as rights and freedoms, fortified with the guarantee of non-discrimination. The article provides:

‘The enjoyment of the rights and freedoms set forth in this Convention shall be secured without discrimination on any ground such as sex, race, colour,

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<sup>639</sup> Vandevelde made a remark on the role of BITs that while they profess as instruments of liberal investment policy, they could only do so in a limited manner. He outlined three principles, namely investment neutrality, investment security and market facilitation which are necessary for the purpose. He concluded that the BITs are geared towards investment security (or protection) reflected in the various provisions including the expropriation clause, fair and equitable treatment (FET), national treatment, most favoured nation treatment (MFN) and full protection and security. Vandevelde, *Bilateral Investment Treaties* (n 2) 109.

<sup>640</sup> Right to property is also established in case laws. In the case of *Marckx v Belgium*, the court held, ‘By recognising that everyone has the right to the peaceful enjoyment of his possessions, Article 1 (P1-1) is in substance guaranteeing the right of property.’ See *Marckx v. Belgium*, (App.6833/74), 13 June 1979, ECHR 1979.



language, religion, political or other opinion, national or social origin, association with a national minority, property, birth or other status.”

The case laws adopt a straightforward test in determining whether a measure has illegitimately discriminated and infringed the right of the claimant on his property without further recourse to achieve a more complex aim such as liberalisation of trade or achieving an internal market.<sup>641</sup> In the ECHR case *Chassagnou and Others v France*<sup>642</sup> for instance, the tribunal has taken a direct assessment of whether there was discriminatory treatment (treatment between small and large land owners) and whether there was objective and reasonable justification (the need to promote the rational management of game stocks). The analytical perspective was whether the discriminatory treatment would infringe the property right (the right to use their lands in accordance to their conscience). On a more general note, it gears towards how to preserve fundamental human rights when they meet public interest.

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<sup>641</sup> The aims of GATT and EU are reflected strongly in the interpretation of its texts. This could be compared to the EU law for instance, which final aim is economic integration. It provides free establishment and free movement of capital to achieve the economic purpose. The EU pursues economic integration in the interpretation of likeness by adopting the *effet utile* principle which is evidenced in the strict interpretation of any derogation. See Article 58 (1)(a) EC and *Manninen* (n 529), para 28). The Court has also placed the attractiveness of the application of the freedoms guaranteed in its analysis of cases. For instance in *Manninen*, the Court construed whether it was less attractive to investors residing in Finland than shares in companies which have their seat in that member state. If a measure results to less attractive application of the treaty, the measure is likely to be incompatible with the EU law. See *Verkooijen*, (n 555), paragraph 35; Case C-334/02 *Commission v France* [2004] ECR I-2229, paragraph 24. Another strong principle in the EU law is ‘direct effect’ which brought to the complete liberalisation (in respect to Directive 88/361) of capital movements and required Member States to abolish all restrictions on such movements. See *Verkooijen*, (n 555), para 33. Similarly, GATT/WTO has its own trade objectives to liberalize trade between WTO member states. The dimension of national treatment assessment has thus been on the competitive performance of the products by the consumers looking into factors such as physical similarities, tariff classifications and the end uses. See Border Tax Adjustments, 2 December 1970, GATT B.I.S.D (18<sup>th</sup> Supp). Due to the competitive nature of the products (competing the same pool of consumers), there is a tendency of assessing the aims of the measure in the angle of protectionism- note ‘so as to afford protection’ in Article III. Although protectionism is equally undesirable in international investment law and that the national treatment is capable to significantly curtail protectionism, this research submits that it could not be elevated to be the underlying philosophy of national treatment. See elaboration in Ch. 3.

<sup>642</sup> *Chassagnou and Others v. France* [GC], nos. 25088/94, 28331/95 and 28443/95, ECHR 1999-III.

There is a commonality in this aspect. Both jurisprudences aim at protecting the right to property and non-discrimination.<sup>643</sup> The interpretation of national treatment has also been straight in cases, even in the deeper integrated treaties like the NAFTA. For instance in the case of *SD Myers*,<sup>644</sup> the tribunal highlighted that the context of the interpretation of national treatment should include consideration that ‘states should be avoiding distortions to trade’. The tribunal then concluded that likeness should be construed whether the investors were in the same sector. This assessment, although motivated by the NAFTA’s aim towards liberalisation, nevertheless provides a plausible criterion of likeness that would be delivered by any other tribunal based on any other treaty. Similarly, in the case of *CPI Inc. v Mexico*,<sup>645</sup> the tribunal underlined the objectives of NAFTA in construing likeness which includes ‘to promote fair competition’ and ‘to increase substantially investment opportunities’. However the primacy of these objectives was not fully tested against a strong grounded regulatory measure. The government measure in this particular case was a countermeasure action which was held by the tribunal to be irrelevant to its national sugar crisis. From the cases, it could be seen that the focus of the tribunals was to protect the investment of the foreign investors against irrational government measures.

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<sup>643</sup> The IHR and IIL jurisprudence despite having similarities in protecting properties nevertheless evolve in isolation resulting to distinct approaches and usage of terminologies between them. Both jurisprudences protect immovable property and tangible assets. See Kriebaum and Schreuer, ‘The Concept of Property in Human Rights Law and International Investment Law’ (n 605); Ursula Kriebaum, ‘Foreign Investments & Human Rights - The Actors and Their Different Roles’ (2013) 10 Transnational Dispute Management (TDM) <<http://www.transnational-dispute-management.com/article.asp?key=1925>>, accessed on 24 January 2013.

<sup>644</sup> *S.D. Myers Inc. v Canada*, (n 24), para 247.

<sup>645</sup> *CPI Inc. v Mexico*, (n 98), para 113. Thus, even with such explicit provision, the effect in the cases so as to depart NAFTA cases from the others is not explicit. Furthermore, deference to the host states are given in a number of NAFTA cases.

There is however one observation that is worth noting. While the international investment law is more geared towards providing a level playing field for the foreign investors to invest in the host state, the ECHR seems to be a level ahead. The non-discrimination principle is often invoked and applied to support ‘equality’ especially in strict scrutiny matters such as discrimination based on gender, race and nationality. However as the subsequent discussion will reveal, in matters which the member states receive wide margin of appreciation, this philosophy seems to dilute and especially where there is no mass number of comparators in which equality could be bench marked.<sup>646</sup>

#### **4.0 Restriction Clause in the ECHR – Scope of Application Compared**

The straddle between the member states regulatory measure and discrimination in the ECHR is however more apparent than in investment disputes. This is due to the explicit restriction clause in the ECHR which calls for a balance in the application of property rights. One may wonder that as the right to property is considered as a fundamental right in ECHR, the protection that entails would be near exhaustive.<sup>647</sup>

On the contrary, the right to property granted in A1P1 is accompanied with a clear restriction clause which words:

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<sup>646</sup> There are some attempts to bring equality as the underlying philosophy and thus criticised the ECHR approach in handling cases as not heading to that direction. The criticism is that Article 14 being narrow and ‘parasitic’, the problematic application of the comparability test. Rory O’Connell, ‘Cinderella Comes to the Ball: Art 14 and the Right to Non-discrimination in the ECHR’ (2009) 29 *Journal of Legal Studies* 211.

<sup>647</sup> As a fundamental right, it would curtail that its infringement would be more grievous than an ordinary infringement or violation. This was illustrated in Janneke H Gerards, ‘The Prism of Fundamental Rights’ (2012) 8 *European Constitutional Law Review* (EuConst) 173. Dupuy emphasised on the origin of the rights to show the fundamental nature of human rights as compared to investment law. While the rights in international investment are directly linked to the state from which the investors received, the human rights are inherent as human being. Dupuy, Francioni, Petersmann, and Dupuy, ‘Unification Rather than Fragmentation of International Law? The Case of International Investment Law and Human Rights Law’ (n 605) 45.

‘The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.’

This means that the right to property is limited if the State sees it necessary for the general interest with a specific mention on ‘payment of taxes’. Similar language is contained in the American Convention on Human Rights in Article 21 which grants individuals the right to use and enjoy property, but it also states that the law may subordinate such use and enjoyment to the interest of society. In *Sporrong Lonnroth v Sweden*, the Court emphasised the challenge to achieve the ‘fair balance which should be struck between the right to property and the requirement of general interest.’<sup>648</sup>

The absence of a restriction clause contrasting the rights of foreign investors rings the question of whether the extent of national treatment protection in investment treaties is wider than the ECHR.<sup>649</sup> The question remains, is it all about property that such restriction is seen in the ECHR or is it related to the ECHR in particular? Could the wide margin of appreciation be applied in the international investment law because of the nature of property?

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<sup>648</sup> *Case of Sporrong and Lonnroth v Sweden* Judgment (Application No. 7151/75; 7152/75) 18 December 1984, para 74.

<sup>649</sup> For example in the context of expropriation in Article 1110 NAFTA, there is a clear guarantee against deprivation of property without explicitly guaranteeing control of the use of property to the states as contained in the ECHR.

These questions influence the scope of national treatment. While it is true that property by itself contains social function, the wide margin of appreciation given to member states in the ECHR was also the result of the member states' compromises. Those compromises gave birth to the restriction or deprivation clause in A1P1 despite its controversial beginning.<sup>650</sup> It is submitted that although such negotiation is absent or not known in the promulgation of investment treaties neither in the texts, it does not negate the importance of deference to host states when there is legitimate public need. Assessing the justification of host states' regulatory measure is inherent in the finding of justifying a claim of discrimination. Deference is given to host states in several cases for instance *Feldman v Mexico*,<sup>651</sup> *Paushok v Mongolia*<sup>652</sup> and *El-Paso v Argentina*<sup>653</sup> as will be explained in the subsequent sections on margin of appreciation. What is absent is the explicit recognition of the status of deference that may provide a significant difference in the way cases are construed.

The ECtHR in this respect therefore has two important guides for the scope of discrimination, firstly the restriction clause (including payment of taxes which would be relevant in investment tax related cases) and the application of margin of appreciation. It follows that Strasbourg determines the rights to be protected (as contained in the ECHR) and it is the contracting parties that determine how to apply them, depending on the suitability of the domestic interests.<sup>654</sup>

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<sup>650</sup> This right was however controversial that it was not incorporated in the ICCPR (except in its discrimination clause) or the ICESCR, but instead incorporated in the regional instruments of IHR as that of ECHR, ACHR and ACHPR. The debate could be seen in the *travaux préparatoire* of the ECHR. See Preparatory Work on Article 1 of the First Protocol to The European Convention on Human Rights, CDH(76)36, Strasbourg, 13 August 1976.

<sup>651</sup> *Feldman v Mexico*, (n 15).

<sup>652</sup> *Sergei Paushok, CJSC Golden East Company, CJSC Vostokneftegaz Company v The Government of Mongolia* UNCITRAL, Award on Jurisdiction and Liability 28 April 2011.

<sup>653</sup> *El Paso v Argentina*, (n 173).

<sup>654</sup> Aaron Baker, 'Proportionality and Employment Discrimination in the UK' (2008) 37 Industrial Law Journal 305.

## 5.0 Likeness

In determining discrimination cases, the ECtHR generally takes into cognisance four prime elements; differential treatment, the comparability of the comparators, objectivity and reasonableness of the measure and proportionality. These elements of discrimination are not treaty based or explicitly required by the treaty in Article 14, but has rather evolved judicially in cases. The *Belgian Linguistics* case in 1968 has laid a foundation of the concept of discrimination which was later referred to by subsequent cases. The court carefully explains the concept of discrimination in the following words:

‘On this question the Court, following the principles which may be extracted from the legal practice of a large number of democratic States, holds that the principle of equality of treatment is violated if the distinction has no objective and reasonable justification. The existence of such a justification must be assessed in relation to the aim and effects of the measure under consideration, regard being had to the principles which normally prevail in democratic societies. A difference of treatment in the exercise of a right laid down in the Convention must not only pursue a legitimate aim: Article 14 (art. 14) is likewise violated when it is clearly established that there is no reasonable relationship of proportionality between the means employed and the aim sought to be realised.’<sup>655</sup>

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<sup>655</sup> Case "Relating to Certain Aspects of the Laws on the Use of Languages in Education in Belgium" v. Belgium (Merits)(Application No 1474/62; 1677/62; 1691/62; 1769/63; 1994/63; 2126/64).

It inferred that not all discriminatory actions are prohibited. A discriminatory action is considered violating equality treatment if it is not objective and justifiable. This case also established the use of proportionality in assessing discrimination. In *Thlimmenos v Greece*,<sup>656</sup> the right not to be discriminated guaranteed in the Convention is only violated when states,

‘...treated differently persons in analogous situations without providing an objective and reasonable justification, but also when States, without an objective and reasonable justification, failed to treat differently persons whose situations were different.’

The *Thlimmenos* case and almost all other discrimination cases reiterated the importance of comparability test in construing Article 14, in similar language or meaning. For instance, in the case of *Efe v Austria*,<sup>657</sup> the court held that it must be established that ‘other persons in an analogous or relevantly similar situation enjoy preferential treatment’.<sup>658</sup> In *Lithgow v United Kingdom* the Court maintained that Article 14 safeguards persons (including legal persons) who are "placed in analogous situations" against discriminatory differences of treatment.<sup>659</sup>

The general trend of assessing likeness can be seen from the words in *Chabauty v France*.<sup>660</sup>

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<sup>656</sup> *Thlimmenos v Greece* (Application No. 34369/97) Decided on Merits, 6 April 2000.

<sup>657</sup> Case of *Efe v Austria* Judgment (Application No. 9134/06) Merits and Just Satisfaction, 8 January 2013.

<sup>658</sup> *Ibid.*, para 43, This principle is applied across A14 cases, see Case of *Unal Tekeli v. Turkey* Judgment (Application No. 29865/96) 16 November 2004, para 49, *Case of the National & Provincial Building Society, the Leeds Permanent Building Society and the Yorkshire Building Society v. the United Kingdom* Judgment (Application No 117/1996/736/933-935) 23 October 1997.

<sup>659</sup> *Lithgow and Ors v UK* Judgment, 8 July 1986, (Application No. 9006/80; 9262/81; 9263/81; 9265/81; 9266/81; 9313/81; 9405/81) para 177.

<sup>660</sup> *Case of Chabauty v France* Judgment (Application No. 57412/08) 4 October 2012.

49. The Court reiterates in this regard that a difference in treatment is discriminatory if it “lacks objective and reasonable justification”, that is, if it does not pursue a “legitimate aim” or if there is not a “reasonable relationship of proportionality” between the means employed and the aim sought to be realised. The Contracting States enjoy a certain margin of appreciation in assessing whether and to what extent differences in otherwise similar situations justify a difference in treatment. The scope of the margin of appreciation will vary according to the circumstances, the subject matter and its background (see, among many other authorities, *Chassagnou and Others*, cited above, § 91, and, for a recent reference, *Konstantin Markin v. Russia* [GC], no. 30078/06, §§ 125-26, 22 March 2012).

There are at least two observations in relation to the comparability test in the ECtHR. Firstly, the construction of likeness in discrimination cases is very brief. Secondly, in many cases the comparability test has not evolved independently, but merged into the justification test.<sup>661</sup> These features are apparent in the ECtHR discrimination cases.<sup>662</sup>

### *5.1 Brief Construction of Likeness*

The ECtHR is less rigorous in the construction of its comparability test despite the resonance of its importance in the cases. If the length of analysis is measured

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<sup>661</sup> There are even instances that it has merged into the differential treatment test. See also Stephen Livingstone, ‘Article 14 and the Prevention of Discrimination in the European Convention on Human Rights’ [1997] *European Human Rights Law Review*, where it maintains that there are three elements to A14 – differential treatment, legitimate aim and proportionality- and that the comparability test is subsumed in the differential treatment test.

<sup>662</sup> F Van Dijk, F Van Hoof and A Van Rijn (eds), *Theory and Practice of the European Convention on Human Rights: Fourth Edition* (4th edn, Intersentia 2006).



between the jurisprudences, it would be clear that investment and trade cases tend to deal more in the comparison analysis. A noticeable stand taken by the court is that if the substantive provision which Article 14 is dependant to is breached, the court will generally not analyse Article 14 for a separate ruling. An example of this is in the case of *Herrmann v Germany*,<sup>663</sup> where there was already a breach of A1P1.<sup>664</sup> Had the court construed likeness, it would be interesting to see how the court would construe the claimant against two comparators, firstly, against owners of real property that do not belong to a hunting district (the enclaves) and secondly the owners of small landholdings.<sup>665</sup> Other examples of brief assessment of likeness are *Fredin v Sweden*,<sup>666</sup> where the Court rejected the similarity between the claimant's gravel pit and at least two others without elaborating the reasons and the case of *Vistinš and Perepjolkins v. Latvia* where the Court similarly rejected the likeness of two acquired lands on the ground of one being 'donated' and the other 'purchased'.

Another observation that may lead to this is that in ECHR cases, the analogy is often made between repeated type of cases or because of the clear similar circumstances of the claimant and the rest of the comparators. Claims are often against a piece of legislation which affect a mass group of people or entities in matters such as pensions, benefits, allowances or personal taxes which would normally provide the court with obvious similarities among the comparators. It is unless if the similarity is unclear, then the court would adopt a more rigorous approach in construing

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<sup>663</sup> *Herrmann v Germany* Judgment (Application No. 9300/07) 26 June 2012.

<sup>664</sup> *Ibid.*, para 94. The court held that the obligation to tolerate hunting has interfered the enjoyment of peaceful possession of the claimants land.

<sup>665</sup> The Chamber earlier decided that there was no violation of A14 read together with A1P1 accepting the justification brought by the government in ensuring the effective management of game stocks and the existence of 'specific situation' of the enclaves. The comparator analysis was not however elaborated. *Ibid.*, para 96.

<sup>666</sup> *Case of Fredin v Sweden Judgment* (Application No. 12033/86) 18 February 1991.

comparability. This could be seen in the more rigorous approach in *Posti and Rahko* which involves comparability between coastal and open sea fishermen.<sup>667</sup> The comparability test is often to disprove similarity of what is otherwise similar, or when the court is not convinced with the similarity. The situation is different in investment dispute cases as the tribunals sought similarity from the very start to prove prima facie case of similarity.

## 5.2 Merging Assessment of Likeness in Justification Test

A plausible logic of this approach is that at most of the time the comparability test links and relates to the objectivity of the regulatory measure which affects the comparability in question.<sup>668</sup> Some commentators view that by taking into account objective justifications as a factor of distinction, it as a way to enhance a meaningful assessment of likeness.<sup>669</sup> Furthermore, since differential treatment can only be prohibited if it has no objective or reasonable justification, the measures have to be scrutinised under that direction.<sup>670</sup> However, this could not hold true for every case. There is danger in the over-use of this approach. As some ECHR cases have indicated, merging the comparability test into justification may cause clear difference or clear similarity of the comparators ignored but the discrimination justified.

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<sup>667</sup> More cases which involve similar investment activities which could be found in investment disputes are normally brought under A1P1, for instance *Marini v Albania* (the court dropped the case under Article 14 for lack of evidence). Case of *Marini v Albania* Judgment (Merits and Just Satisfaction) (Application No. 3738/02) 18 December 2007; *Case of Posti and Rahko v. Finland* Judgment (Application No. 27824/95) 24 September 2002.

<sup>668</sup> Dijk, Hoof, and Rijn, *Theory and Practice of the European Convention on Human Rights* (n 662) 1036

<sup>669</sup> *Ibid.*

<sup>670</sup> *Case of Raviv v Austria* Judgment (Application No. 26266/05) 13 March 2012, para 47.

The merging of comparability test into justification test would also result to decisions that two comparators are not alike because of the very ground upon which discrimination is alleged.<sup>671</sup> In the case of *Posti and Rahko v Finland*,<sup>672</sup> the aim of the measure was not disputed – that the measure was needed to ‘safeguard relevant fish stock, taking into consideration different fishing gear and different timing of spawning route’. What was disputed was the discriminatory effect the measure causes to coastal fishermen as opposed to open sea fishermen. The court held that they were not alike for the exact same reason the measure was introduced. This may not be as controversial where cases which have obviously or deliberately resorted to the justification of the measure as a basis of distinction.<sup>673</sup>

In the ECHR context, this inconsistency has been criticised for being politicised in what has led it to a restrictive application.<sup>674</sup> Criticisms occur in both approaches, excessive merging of comparator test into justification test and the over reliance of the comparator test, especially when there is no objective justification to defend the measure.<sup>675</sup>

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<sup>671</sup> McColgan, ‘Cracking the Comparator Problem: Discrimination, Equal Treatment and the Role of Comparisons’ (n 95).

<sup>672</sup> *Posti and Rahko v. Finland*, (n 667).

<sup>673</sup> Joory, ‘Arguments against the Politicized Role of Comparators in Article 14 Discrimination Cases’ (n 95).

<sup>674</sup> *Ibid.*; Gerards, ‘The Discrimination Grounds of Article 14 of the European Convention on Human Rights’ (n 134).

<sup>675</sup> McColgan, ‘Cracking the Comparator Problem: Discrimination, Equal Treatment and the Role of Comparisons’ (n 95). In particular the *Case of Carson and Others v. The United Kingdom* Judgment (Application No.42184/05) 16 March 2010.

### 5.3 Extracted Criteria of Likeness

The most obvious methodology in assessing likeness in ECHR is the application of concepts of margin of appreciation and proportionality. These two concepts in the determination of likeness will be looked at extensively in the subsequent sections. In this section, certain other noticeable characteristics which may be intrinsic to the different set of facts of the cases are worth noting. These criteria which are extracted may be a useful guidance for international investment national treatment cases:

1. *The Detriment Factor*: This approach may seem similar to the assessment of less favourable treatment, but it does not bring the same effect when applied under the examination of likeness. While less favourable treatment requires the proof of treatment below the level accorded to the locals, the detriment test requires the examination of discriminatory effect which could indicate the unlikeness of the situation of two investments facing a single regulatory measure. This approach is essentially important if a regulatory measure provides a general measure that by *de facto* cause detrimental and discriminatory impact to a particular investment. Here, the characteristics of the investment may not be enough to represent the unlikeness of the investments, but the situation caused by the detrimental impact could.

In the case of *Posti and Rahkov Finland*,<sup>676</sup> a fishing restriction which was imposed to both coastal and open-sea fishermen was challenged by the coastal fishermen as discriminatory. The restriction was aimed to safeguard

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<sup>676</sup> *Posti and Rahko v. Finland*, (n 667).

the relevant fish stocks as seen in the restrictions of the different timings, different water areas and the different fishing gears taking into account the spawning routes of salmon. The court attempted to examine the detrimental impact as alleged by the applicant and found no differential of treatment in that regard.

Such situations would occur more in the context of international human rights law as the doctrine of non-discrimination explicitly covers both treating likeness unlike and treating unlike alike.<sup>677</sup> In the international investment law, although most investment treaties specify the prohibition to treat like investments unlike, it does not mean to confine like investments to investments similar in characteristics or sector per se, but extended to the situation of the investments. Thus, in certain situations of de facto discrimination it may require the claimant to indicate the detriments caused by the measure to the investment as compared to the comparator. It may be even more relevant in treaties which do not clearly specify 'like investments'.

This approach is also relevant when the underlying justification of the regulation is not disputed as in *Posti and Rahko v Finland*, but the overall policy which nevertheless at the end discriminates a particular group. At this particular point, discussions on the rational aim of the measure may no longer be necessary but other matters must also be scrutinised, including the

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<sup>677</sup> The ECHR is violated not only when States – without providing an objective and reasonable justification – treat differently persons in analogous situations but also when they fail to treat differently persons whose situations are significantly different (see *Thlimmenos v. Greece* (n 656)).

manner, the reasonable relationship of proportionality<sup>678</sup> or even the detrimental impact which may cast further indication of the likeness of situation. Thus the justification sought should shift as to why equal treatment is given despite the discriminatory and detrimental impact. This also reflects the philosophy of equality, as equality does not necessarily mean equal treatment but a treatment that is fair taken into account the circumstances of those imposed upon.

2. *Identifiable Characteristics*<sup>679</sup>: Two comparators which are generally alike must not be regarded unlike in the absence of any identifiable characteristic. In the case of *B v UK*,<sup>680</sup> the government required the claimant to repay a sum of overpaid benefit upon a disclosure of fact. The claimant alleged that the government has discriminated unjustifiably between capable and incapable people who could understand the facts which they are required to report. The court accepted the dissimilarity between two situations of mental capacity. The court highlighted that in its case law, only differences in treatment based on an identifiable characteristics or status can be regarded as discrimination.<sup>681</sup>

3. *Correction of Factual Inequalities*: The Court does not prohibit discrimination in order to correct factual inequalities. However such correction of factual inequalities must be with objective and reasonable

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<sup>678</sup> *Case of Kuric and Others v Slovenia* Judgment (Application No. 26828/06) 26 June 2012, para 386.

<sup>679</sup> *Raviv v Austria*, (n 670), para 46; *Case of Carson and Others v. The United Kingdom* Judgment (Application No.42184/05) 16 March 2010.

<sup>680</sup> *Case of B v United Kingdom* Judgment (Merits and Just Satisfaction) (Application No. 36571/06) 14 February 2012.

<sup>681</sup> *Ibid.*, para 54.

justification.<sup>682</sup> The decision in *El-Paso v Argentina* has indirectly applied this concept. Due to the economic crisis, the government attempted to re-balance the situation of banking sector as opposed to exporters including oil and gas companies which have benefited from the devaluation of peso. The tribunal stated:

‘The Tribunal also takes note of a statement made by the Claimant itself, making the same analysis when saying that “those who export their production ... benefited from the devaluation of the Peso since the Peso equivalent value of their exports tripled.” It was thus reasonable for the Government to institute a tax on the unexpected profits made by the oil and gas companies to re-balance the situation of the banking sector. Far from being discriminatory, this measure aimed at equalising the playground of the different economic actors, by distributing more equitably the burden of the country’s economic crisis among all those affected.’<sup>683</sup>

This test would trigger many hypothetical situations in investment disputes which involves better treatment of less advantaged local groups. Presumably, if the state provides subsidies to smaller farms or industry, or to investments which have not yield investment returns as compared to foreign investment which already have repeatedly, it would be allowed under this test. Should this test be invoked and applied, the assessment of proportionality must follow with great scrutiny.

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<sup>682</sup> See *Thlimmenos v Greece* (n 656).

<sup>683</sup> *El Paso v Argentina*, (n 173), para 314.

## 6.0 Principles Applied Throughout Determination of Likeness

It is indicated earlier that there are concepts emphasised by the ECHR in discrimination assessments. These are the concepts of margin of appreciation and the reasonable relationship of proportionality between the means employed and the aim sought to be realised.<sup>684</sup> This standard of review is emphasized throughout the jurisprudence.<sup>685</sup>

### 6.1 Margin of Appreciation

The introduction of margin of appreciation in Art 14 found its way in the case of *Belgian Linguistics*.<sup>686</sup> The rationale of margin of appreciation is to acknowledge that the state is in the position to know better what is in the better interest of the public or the economic situation than the Court.<sup>687</sup> It is a method to respect the legislature's assessment.<sup>688</sup> The court has generally guided its application based on the grounds put forth in the cases.<sup>689</sup> A narrow application of margin of appreciation

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<sup>684</sup> *Case of Andrle v. the Czech Republic* Judgment (Application No. 6268/08), 17 February 2011 para 48.

<sup>685</sup> Dirk Ehlers and Dr Ulrich Becker, *European Fundamental Rights And Freedoms* (Walter de Gruyter 2007) 93–94.

<sup>686</sup> Howard C Yourow, *The Margin Appreciation Doctrine in the Dynamics of European Human Rights* (Martinus Nijhoff Publishers 1996) 29.

<sup>687</sup> *Case of Lithgow v United Kingdom* Judgment (Merits) (Application No. 9006/80; 9262/81; 9263/81; 9265/81; 9266/81; 9313/81; 9405/81) 8 July 1986, para 122, *Andrle v. Czech Republic*, (n 684), para 50.

<sup>688</sup> *National & Provincial Building Society, the Leeds Permanent Building Society and the Yorkshire Building Society v. The United Kingdom*, (n 658), para 80.

<sup>689</sup> The doctrine was developed on a case by case basis. See Oddný Mjöll Arnardóttir, *International Studies in Human Rights, Equality and Non-Discrimination Under the European Convention on Human Rights* (Martinus Nijhoff Publishers 2003) 63.



is given to states in discrimination relating to race, colour or ethnic diversity<sup>690</sup> and in the sphere of family life.<sup>691</sup> On the other hand, a wider margin of appreciation is given in matters of nation's security and military,<sup>692</sup> the determination of social security system,<sup>693</sup> the economic and social policy.<sup>694</sup>

The margin of appreciation accorded to the states in the matter adjudged determines the scope of protection guaranteed under A1P1 and Article 14 ECHR.<sup>695</sup> It plays a significant role in determining whether two comparators are alike. In the case of *Stummer v Austria*, the court mentioned:

‘The Contracting States enjoy a certain margin of appreciation in assessing whether and to what extent differences in otherwise similar situations justify a different treatment.’<sup>696</sup>

In the *Case of the National & Provincial Building Society, the Leeds Permanent Building Society and the Yorkshire Building Society v. the United Kingdom*,<sup>697</sup> the

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<sup>690</sup> See, among many other cases *Case of Oršuš and Others v. Croatia* Judgment (Application No. 15766/03) 16 March 2010 and *Case of Kuric and Others v Slovenia* Judgment (Application No. 26828/06) 26 June 2012, para 386.

<sup>691</sup> *Case of Konstantin Markin v Russia* Judgment (Merits and Just Satisfaction)(Application No.30078/06) 22 March 2012, para 100.

<sup>692</sup> *Ibid.*, para 134.

<sup>693</sup> *B v United Kingdom*, (n 680), para 50.

<sup>694</sup> *Efe v Austria* (n 657), para 36, *Case of Stummer v Austria* Judgment (Merits and Just Satisfaction) (Application No. 37452/02), 11 October 2007, para 89. This includes ‘general measures of economic and social strategy’, see *Andrle v. Czech Republic*, (n 684) para 50; *Case of Zubczewski v Sweden* Decision as to Admissibility (Application No. 16149/08) 12 January 2010 para 15; *Case of Andrejeva v Latvia* Judgment (Merits and Just Satisfaction) (Application No. 55707/00) 18 February 2009.

<sup>695</sup> See *Case of Gaygusuz v Austria* Judgment (Merits and Just Satisfaction)(Application No.17371/90) 16 September 1996, *Case of Rasmussen v Denmark* Judgment (Merits) (Application No.8777/79) 28 November 1984, and *Case of Inze v Austria* Judgment (Merits and Just Satisfaction) (Application No. 8695/79) 28 October 1987.

<sup>696</sup> Similar wordings are repeated in *National & Provincial Building Society, the Leeds Permanent Building Society and the Yorkshire Building Society v. The United Kingdom* (n 658), para88, and *Case of Stubbings and Others v The United Kingdom* Judgment (Merits) (Application No. 22083/93; 22095/93) 22 October 1996.

<sup>697</sup> *Ibid.*

claimant attempted to recover sums paid in application of invalidated fiscal provisions alleging that it was in similar situation with another company called Woolwich. The court applied margin of appreciation in ruling that there was reasonable and objective justification by public interest to secure liability to tax and the intention of the Regulation to make it immune from any other exploitation on technical grounds. Woolwich has also mounted a legal charge which made it incomparable to the claimant. The court held:

‘The decision to do so retrospectively has been found by the Court to be justified in the public interest (see paragraph 81 above). To exclude the Woolwich from the retroactive effect of section 53 could be considered on reasonable and objective grounds to be justified given that by the time of enactment of that section the Woolwich had secured a final judgment in its favour from the House of Lords and it was understandable that Parliament did not wish to interfere with a judicial decision which brought to an end litigation which had lasted over three years.’<sup>698</sup>

#### *6.1.1 Wide Margin of Appreciation in Property Matters v Strict Scrutiny for Ground of Nationality*

It must be noted that although a wide margin of appreciation is given to member states in the matter of property, the ECHR construed stricter scrutiny of the state’s actions if it involves discrimination based on nationality. Especially in suspect grounds category (which includes discrimination based on sex, race, nationality), the

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<sup>698</sup> *Case of the National & Provincial Building Society, the Leeds Permanent Building Society and the Yorkshire Building Society v. the United Kingdom*, (n 658), para 90.

court would require for weighty reasons for any justification put forth by the states.<sup>699</sup> In the case of *Gaygusuz v Austria*, a Turkish who worked in Austria applied for an advance on his pension in the form of emergency assistance but was rejected on the ground that he did not have Austrian nationality. The court applied a stricter scrutiny on the measure and found no objective and reasonable justification.<sup>700</sup> It was therefore held that Mr. Gaygusuz was in like situation to Austrian nationals as regards to his entitlements.<sup>701</sup>

Although the subsequent cases have upheld strict scrutiny test on cases based on nationality in cases of regular migrants,<sup>702</sup> they could not hide the fact that the issue of discrimination based on nationality is complex and sensitive<sup>703</sup>. Especially in addressing problems of non-nationals benefitting welfare programmes, questions of national interest and limited resources intended for nationals has arisen. This has also triggered the theoretical understanding of discrimination between ‘universalism and particularism’ on whether equality should be enjoyed by all human beings or only by the people belonging to a constituted liberal polity.<sup>704</sup> The latter would correspond to

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<sup>699</sup> The high scrutiny approach in certain matters (important personal liberties as opposed to legislations that regulate ordinary economic activity) is adopted from/ more popular in the US by Stone J in *Carolene Product* case. See *United States v Carolene Products Co* 304 US 144, 58 S Ct 778 (1938).

<sup>700</sup> *Gaygusuz v Austria*, (n 695), para 50.

<sup>701</sup> *Ibid.*, para 48.

<sup>702</sup> *Case of Koua Poirrez v France* Judgment (Merits and Satisfaction) (Application No. 40892/98) 30 September 2003; *Andrejava v Latvia* Application No 55707/00; Merits and Just Satisfaction, 18 February 2009 ; *Case of Luczak v Poland* Merits and Just Satisfaction (Application No 77782/01) 27 November 2007.

<sup>703</sup> See dissenting opinion in *Gaygusuz* which reveals the sensitivity of the issue of immigration and the abuse of the welfare system. Judge Matscher remarked,

‘The background to the whole case is a typical instance of abuse of the Welfare State, a very widespread trend in all our societies and one - I would point out - by no means limited to foreign workers. It is regrettable that the Court, by awarding disproportionate amounts of compensation, should reinforce this trend.’

*Gaygusuz v Austria*, (n 695), Partially Dissenting Opinion of Judge Matscher.

<sup>704</sup> Marie-Bénédicte Dembour, ‘Gaygusuz Revisited: The Limits of the European Court of Human Rights’ *Equality Agenda* [2012] *Human Rights Law Review* 3 <<http://hrlr.oxfordjournals.org/content/early/2012/12/12/hrlr.ngs025>> accessed 27 February 2013.

the power of the state to determine sensitive national concerns hence granting a wider margin of appreciation to the member states.<sup>705</sup>

In a deeply rooted nationality based investment treaties (i.e the NT provision and the admissibility of investment cases which require the establishment of nationality), the adoption of the *Gaygusuz* approach would defy the meaning of its adjudication, rendering an easy superfluous approach towards the protection of foreign investors. It will also negate the mantra of both the ECHR and investment treaties – that not all discrimination is a violation, when there is a rational for the measure. This is the exact function of objective and reasonable justification test in the ECHR and the rational policy and legitimacy test in investment arbitrations. Nationality by itself should not be the one and definitive element to strike out any government action as shown in *Gaygusuz*. It must also be noted that national based discrimination cases in the international human rights law are generally broader than investment law, including employment,<sup>706</sup> elections,<sup>707</sup> social securities and pensions. These are socio-economic aspects which are prone to apply the principle of non-discrimination to achieve ‘equality’ in the society.

*Gaygusuz* however, may be helpful in emphasizing the fragility of the status of non-nationals in facing regulatory measures that may be nationally biased. The lesson

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<sup>705</sup> See Marc Bossuyt, ‘Should the Strasbourg Court Exercise More Self-Restraint? On the Extension of the Jurisdiction of the European Court of Human Rights to Social Security Regulations’ (2007) 28 Human Rights Law Journal 321. This is also in line with the principle of non-discrimination under customary international law. Borzu Sabahi has discerned from the U.S Restatement 1987, section 712 that the principle of non-discrimination sanctions unreasonable distinction but exempted nationality based classification for security or economic purposes. Borzu Sabahi, ‘National Treatment-Is Discriminatory Intent Relevant?’ in Todd Weiler (ed), *Investment Treaty Arbitration and International Law* (JurisNet 2008) 270.

<sup>706</sup> *Syndicat National des Professions du Tourisme v France* (Complaint no. 6/1999) 10 October 2000 ECSR.

<sup>707</sup> *Case of Karakurt v Turkey* Judgment (Merits and Just Satisfaction) (Application No. 45718/99) 20 September 2005.

learnt is perhaps the level of scrutiny that is required. It is to ensure that whilst the government can exercise its margin of appreciation, the measure is not aimed at ‘singling out’ foreign investors due to nationality by way of examining the design and structure of the measure. Thus the host state’s measure must not only be objective and reasonable, it must also not be designed to discriminate foreign investors.

### *6.1.3 Excessive Use of Margin of Appreciation and Its Effects on Comparability*

The ECHR standard of wide margin of appreciation means that the court can only intervene if it is ‘manifestly without reasonable foundation’.<sup>708</sup> It is counter-checked with the tests of ‘objective and reasonable justification’ and proportionality. This methodology is plausible in determining discrimination. The problem in the ECHR cases is however, that the latter tests were not construed extensively (as one would expect) in matters which are given wide margin of appreciation despite theoretically and conceptually emphasized in cases. This results to an odd effect of margin of appreciation which is reflected in the narrow scope of application of discrimination in the ECHR. For instance, in the case of *Zubczewski v Sweden*, as Swedish national had his pension reduced approximately 50 Euro per month due to his marriage at the age of 63. The state’s reason for this difference of treatment was that married couples who live together generally had lower costs for living per capita than single, unmarried persons.<sup>709</sup> This principle constituted a general measure of the Swedish social and economic strategy. Despite reiterating the importance of objective and

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<sup>708</sup> *Stummer v Austria*, (n 694), para 101.

<sup>709</sup> *Case of Zubczewski v Sweden Decision as to Admissibility (Application No. 16149/08) 12 January 2010, para 15.*

reasonable justifications in its reasoning, the court seemed to disregard the economic dependency of the wife on the applicant that would have made him non-comparable to other married couples. Margin of appreciation was applied exclusively and excessively and has resulted to an absurd comparison of unlike situations which was so self-evident.

Without proper utilisation of objective and reasonable justification test and proportionality, the following result could occur in investment cases (as have been criticised in the ECHR):

- a) In determining comparator, examination of likeness would reduce and would face the risk of being abandoned or ignored. If investment law is to apply the flexibility or wideness of margin of appreciation as given in matters of property, scrutiny of likeness would be at risk as it will be hard to be proven when margin of appreciation is given to the state.<sup>710</sup>
- b) Excessive application of margin of appreciation will expose to the investors to further degree of uncertainty.<sup>711</sup>

#### *6.1.4 Non-exclusiveness of Margin of Appreciation*

Any exercise of margin of appreciation must not be unlimited. The Court has made it clear that it will respect the States' policy unless it is 'manifested without reasonable

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<sup>710</sup> Oddný Mjöll Arnardóttir, 'Non-Discrimination Under Article 14 ECHR: The Burden of Proof' [1999] *Scandinavian Studies in Law* 14.

<sup>711</sup> This has been commented by Jakob Cornides in the context of ECJ cases. See Jakob Cornides, 'Three Case Studies on Anti-Discrimination' (2012) 23 *Eur.J.Int'L* 517.

foundation.’<sup>712</sup> Caution must be made to the powerful effect of margin of appreciation in discrimination assessment. In the context of ECHR, the rationale of strict scrutiny on discrimination on minorities and non-nationals is the fear that the democratic application of margin of appreciation which is made by the majority would jeopardise the minorities and non-nationals under the name of democratically made legislation or measures.<sup>713</sup> Although a measure may be economic in nature (in the realm of wide margin of appreciation), it would still render a narrow margin of appreciation if it is directed to a small group of people (foreign investors or non-nationals). Analogically, in the context of foreign investors, the non-voting rights would expose them to the change of legislations or introduction of measures that are not in their favour. Thus, what could be learnt here is that a wide margin of appreciation is only appropriate when it affects the whole population generally.<sup>714</sup> This could reduce the risk of acknowledging states’ measures which are disguised in a particular public purpose, in the complex realm of public choice theory. This assessment is potentially part of the ‘rationality’ test in investment tribunals, that a measure is not targeted on the foreign investors.

In the context of national treatment especially, deference to host states must be guided as it involves possible protection of domestic investors by way of regulatory measures. Allowing unguided application of margin of appreciation would undermine the purpose of national treatment provision realising the fact that the

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<sup>712</sup> *Andrle v. Czech Republic*, (n 684) para 50; *National & Provincial Building Society, the Leeds Permanent Building Society and the Yorkshire Building Society v. the United Kingdom*, (n 658), para 80

<sup>713</sup> In the context of minorities, it is stated in Benvenisti that ‘Majorities often monopolize political power with little more than half of the votes and thus use the democratic processes as means to secure their interests at the expense of the minority’ See Eyal Benvenisti, ‘Margin of Appreciation, Consensus and Universal Standards’ 31 *International Law and Politics* 843, 848.

<sup>714</sup> *Ibid.*, 847.

regulatory measures could be used as tools for protectionism to the disadvantage of foreign investors. As compared to expropriation, the scrutiny of the objective and reasonableness of the measure in national treatment is paramount due to its potential alteration of the national treatment effect. Similarly in A1P1 of the ECHR, the application of margin of appreciation is not confined or restricted by the additional characteristic of nationality discrimination if it is not accompanied with Article 14 on the ground of nationality. Thus the objective and reasonable justification and the proportionality test in the latter works for both A1P1 and Article 14.

The application of the margin of appreciation must not be unlimited. It must be subjected to certain conditions among which are:

1. That it observes other principles primarily reasonableness, proportionality and good faith.<sup>715</sup>
2. It must not lead to ‘denial of justice’.<sup>716</sup> The application of margin of appreciation must be balanced with the loss of bargaining power that foreign investors face once they have sunk their assets in the host state. Unguided application of margin of appreciation will render the protections in the investment treaties meaningless. It would deny the effective system of justice.

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<sup>715</sup> Yuval Shany, ‘Toward a General Margin of Appreciation Doctrine in International Law?’ (2005) 16 *European Journal of International Law* 907.

<sup>716</sup> Paulsson, *Denial of Justice in International Law* (n 344). See also Loewen. Final Award. Prof. Greenwood 2<sup>nd</sup> Opinion, para 129.



3. That there is no consensus on the matter elsewhere. In the context of ECHR, there must be no existing consensus in the ECHR in the matter of which the government wishes to apply its own judgment.<sup>717</sup> In a joint partly dissenting opinion of the case of *Stummer v Austria*, it was opined that where a trend has emerged in how other states construe a matter, that would reduce the margin of appreciation that a state should enjoy in the area.<sup>718</sup>
4. Whether it involves matters of sovereignty. Even though discrimination on nationality ground receives narrow margin of appreciation in the ECHR<sup>719</sup>, it is not expected that states would lose its discretionary power in immigration matters that involves sovereignty.<sup>720</sup> Most property measures in ECHR cases are on claims on pensions<sup>721</sup>, benefits and these involve ‘domestic variables’<sup>722</sup> and often a mix of ‘economic and social’ consequences in which need a wide margin of appreciation for the member states.

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<sup>717</sup> Benvenisti, ‘Margin of Appreciation, Consensus and Universal Standards’ (n 713); Laurence R Helfer, ‘Consensus, Coherence and the European Convention on Human Rights’ (1993) 26 Cornell International Law Journal 133.

<sup>718</sup> Joint Partly Dissenting Opinion of Judges Tulkens, Kovler, Gyulumyan, Spielmann, Popovic, Malinverni and Pardalos in *Stummer v Austria*, (n 694), para 5.

<sup>719</sup> *Gaygusuz*, (n 695), para 42 and *Koua Poirre v France* (n 702).

<sup>720</sup> Janneke H Gerards, ‘Intensity of Judicial Review in Equal Treatment Cases’ (2004) 51 Netherlands International Law Review 135, 181.

<sup>721</sup> *Andrle v. Czech Republic*, (n 684).

<sup>722</sup> *Andrle v. Czech Republic*, (n 684) para 56.

## 6.2 Reasonable Relation to Proportionality

Proportionality test became the foundation of discrimination assessment of Article 14 ECHR in the case of *Belgian Linguistics*.<sup>723</sup> The proportionality test is to determine whether the state's use of objective justification to distinguish the comparators has outweighed its need. A measure is regarded as not proportionate due to certain factors. The most common is when a measure is objective and justifiable but the method is not proportionate where a particular method is chosen even though less restrictive alternative measures exist. In the case of *Andrle v The Czech Republic*, the court held that the progressive and gradual measure taken by the Czech Republic to compensate the inequality between men and men since socialist Czechoslovakia was proportionate and related to the legitimate objective even though discrimination may remain in a group of people not yet affected by the change. In this case the male applicant complained of discrimination concerning the lowering of the pensionable age for women who took care of children but not for men in the same situation. The court mentioned:

‘Therefore, the State cannot be criticised for progressively modifying its pension system to reflect these gradual changes (see also paragraph 51 above) and for not having pushed for complete equalisation at a faster pace. Indeed, the respondent Government have to choose from among different methods of equalising the retirement age. This task is even more demanding and deserves well-thought-out solutions since the State has to place this

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<sup>723</sup> Case "Relating to Certain Aspects of the Laws on the Use of Languages in Education in Belgium" v. Belgium (Merits)(Application No 1474/62; 1677/62; 1691/62; 1769/63; 1994/63; 2126/64), para 10, Part B.

reform in the wider context of other demographic shifts, such as the ageing of the population or migration, which also warrant adjustment of the welfare system, while preserving the foreseeability of this system for the persons concerned who are obliged to contribute to it.’

ECHR cases have emphasised that a measure must be proportionate when it has to discriminate. This involves claiming why two comparators are not the same or comparable. What is not seen in the ECHR is the use of proportionality to limit comparability especially when it involves conflicts with other rights. In the case of *Test Achats*,<sup>724</sup> Article 5(2) of the Directive 2004/113/ was declared invalid because it allowed the use of gender related factors in determining premiums and benefits under insurance schemes. While the Directive has to be examined whether it is reasonable and proportionate, it is almost neglected that the a test must also be made on whether it is proportionate to rule comparability between male and female in the insurance context, and the economic impact in the insurance industry and perhaps the right to enter into insurance contract based on risk assessment which may be contingent to gender. A more striking conflict with the right to contract can be seen in the case of *Hall & Preddy v. Bull & Bull*.<sup>725</sup> By claiming the discrimination against a homosexual couple who were refrained from a B&B that restricts unmarried couples, the court has indirectly negated the freedom of contract of the B&B owner. In another case, *B v UK*, the court held that governments should be allowed to correct its mistakes in awarding benefits as depriving them from doing so

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<sup>724</sup> Case C-236/09, *Association belge des Consommateurs Test-Achats ASBL, Yann van Vugt, Charles Basselier v. Conseil des ministres* ECJ (Grand Chamber) 1 March 2011.

<sup>725</sup> *Bull & Bull v Hall & Preddy* [2012] EWCA Civ 83 (10 February 2012).

would result to benefits being enjoyed unjustly, contrary to the doctrine of unjust enrichment.<sup>726</sup>

In the ECHR, this principle is more apparently applied on questions of discrimination on certain grounds where the margin of appreciation is narrow. In such cases, the Court imposes the burden to the states to provide ‘very weighty reasons’ so as to the need of such distinction.<sup>727</sup> On the other hand, it is less seen in matters of wide margin of appreciation which has played a more dominant role.

It is submitted that matters which receive wider margin of appreciation needs similar attention with regards to the assessment of proportionality. This would balance the deference given to the state and determine the broader societal impact<sup>728</sup> and the suitability and reasonableness of the methods used by the states to achieve their legitimate aims within their wide margin of appreciation.

### *6.3 Legitimate Expectation*

Legitimate expectation is used to protect substantive expectations about the treatments in investment treaties.<sup>729</sup> However, it is normally applied in fair and equitable treatment (FET) and expropriation. This section explores whether this concept could be applied in the context of national treatment. It is argued that

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<sup>726</sup> *B v UK*, (n 680), para 60.

<sup>727</sup> Gerards, ‘Intensity of Judicial Review in Equal Treatment Cases’ (n 720) 161.

<sup>728</sup> *Belgian Linguistics*, (n 723), para 283.

<sup>729</sup> Newcombe and Paradell, *Law and Practice of Investment Treaties* (n 65) 280. Among the ECHR cases which apply legitimate expectation are *Case of Pine Valley Developments Ltd and Others v Ireland* Judgment (Merits) (Application No. 12742/87) 29 November 1991, para 51 and *Case of Maurice v France* Judgment (Application No. 11810/03) 21 June 2006, para 69.

legitimate expectation could be a useful tool in providing stability and predictability in the assessment of likeness in national treatment.

The first scenario is if the host states have provided certain guarantees for a specific economic sector ensuring that a certain investments are alike to other investments within the group, it is reasonable that the investors would rely on them. This is also in line with the ‘legal similarity test’ in the EU law. For instance, if the host state includes oil pipelines under the same category of ‘common carriers’ in respect of contract rate which includes ferrymen, canal boat owners and stagecoaches, the investors would have a basis to rely on this piece of legislation as a legitimate expectation.<sup>730</sup> Thus if the host state later wishes to regulate or impose different contract rates on oil pipelines on the ground of capacity which would discriminate oil pipelines which has calculable capacity as compared to railroad capacity, it would likely be against the legitimate expectation of the investors unless if it can be proven that there is ‘overriding public interest’ to deprive him from such interpretation. Similarly, if there is a domestic bill or legislation that includes hydroelectric projects as ‘clean energy’ together with other traditional renewable projects like wind, biomass or photovoltaic, it would be a clear case of likeness in the absence of justifications of overriding public interest.<sup>731</sup>

In such situations, it would be easier if there is no legal classification of sectors for the investors to rely on at the first place. The tribunal would only have to examine

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<sup>730</sup> Possible comparability issue that may arise from contract rates on shippers. See Christopher J Bar, ‘Unfinished Business: FERC’S Evolving Standard For Capacity Rights in Oil Pipelines’ (2011) 32 Energy Law Journal 563.

<sup>731</sup> See David C. Coen, ‘Should Large Hydroelectric Projects Be Treated as Renewable Resources’ (2011) 32 Energy Law Journal 541; Mary G Powell, ‘Treatment of Large Hydropower as a Renewable Resource’ (2011) 32 Energy Law Journal 553.

comparability of the oil pipelines and railroad transportation based on their merits. This would also caution host states to be careful in guaranteeing certain advantages in grouped investments or economic sectors that would lure foreign investors unless such categorisation is to be adhered to.

It must be noted that expectations are however not unconditional and everlasting.<sup>732</sup> If the measure is responding to a legitimate public interest, the investors could not hold on to the expectation. This is where the margin of appreciation comes in, but restricted to rationality and proportionality. Indeed in matters involving environment or health, it could be expected that new change of legislation may occur in response of new scientific discoveries.<sup>733</sup> If the state has human rights obligation, it should be expected that the obligation will be fulfilled.<sup>734</sup>

In the absence of legal representations or regulations that guarantee likeness, legitimate expectation on comparability can be ascertained by understanding what would fall under the state's margin of appreciation which are rational and justifiable. Presumably as previously mentioned, sensitive public matters like environment, health and safety would grant the state a wider margin of appreciation. Arguably, economic justifications could also be included under the category depending on the rational of the measure and its proportionality.

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<sup>732</sup> *International Thunderbird Gaming Corporation v The United Mexican State*, UNCITRAL, Separate Opinion of Prof. Thomas Wälde, 1 December 2005, para 30.

<sup>733</sup> Waelde and Kolo, 'Environmental Regulation, Investment Protection and "Regulatory Taking" in International Law' (n 39) 819.

<sup>734</sup> Dupuy, Francioni, and Petersmann, *Human Rights in International Investment Law and Arbitration* (n 604) 54.

It could be reasonably inferred that there is legitimate expectation in the foreign investors that they would not be treated less favourably than comparable domestic investors as argued by the claimant in *Methanex v USA*. The fact that both investors were producing oxygenates, fortified by the existence of competition, should qualify the test of likeness. However, the tribunal chose to adopt a restrictive approach in requiring the ‘most like circumstances’ of situations which are already alike, and ignored the assessment of likeness in view of the claim at hand. If this was construed as legitimate expectation, the task then required from the tribunal is to assess whether there is any rational for the host states to consider the investors as not in like circumstances by applying the margin of appreciation. If there is none, then comparability is established and the assessment of the rational and justifiability of the measure will follow. Though potentially this would result to a more meaningful assessment of likeness, the discussion did not heed towards this direction. Confusingly, while the tribunal rejected the idea of ‘like products’, ‘competitive’ and ‘substitutability’ in GATT/WTO,<sup>735</sup> by adopting the ‘most like circumstances’ or ‘identical’ as there were identical operators, it has similarly brought the assessment to one which is micro and technical which may not be placing the assessment of the ‘circumstances’ of the comparator.

## 7.0 Conclusion

This research suggests that the international human rights jurisprudence could provide an instructive guide by way of analogy.<sup>736</sup> Investment tribunals should

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<sup>735</sup> *Methanex v USA*, (n 19), para 37.

<sup>736</sup> It is discussed elsewhere on the possibility of applying IHR principles in IIL by way of applicable law. It is triggered that general principles of law (Article 38 ICJ Statute) could include the *jus cogen*

benefit from the similar questions asked in the structurally similar individual-states adjudication. The tribunal must have the ability to foresee the result of justice that would come from the decision when applying a particular approach of comparability. This is to avoid absurd result in the end justice. The ECJ approach for instance in the case of *Tadao Maruko v. Versorgungsanstalt der Deutschen Bühnen* was criticised for its failure to recognise the factual differences of same-sex life partners and married couple. By adopting solely the legal similarity, the ECJ has committed ‘logical error’ or ‘*petitio principii*’ and resulted to a judgement that ‘creates no equality but undeserved privileges’. <sup>737</sup> Surely, this echoes the investment decision in *OEPC v Ecuador* where a construction of likeness from one point of view had failed to fit in the logical understanding of likeness which results to an exploration oil company to be in like circumstances with agriculture companies including flowers etc. Although one may argue the role of ‘justice’ in the decision making of investment tribunals, it is submitted that the whole system must not lead to the denial of justice by providing weak standards of interpretation of the protections.

This chapter has explored the basis of reference to the ECHR jurisprudence by outlining ‘protection of rights’ as the underlying principle between the two jurisprudences. It has also highlighted the role of important administrative principles in determining comparators in discrimination cases. The nature of international

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principle of non-discrimination via ‘(and) international law as may be applicable’ in A42 ICSID and ‘applicable rules of international law’ in Article 1131 NAFTA and Article 26 (6) ECT. Dupuy, Francioni, and Petersmann, *Human Rights in International Investment Law and Arbitration* (n 604) 57. The analysis of the word ‘and’ was scrutinised to give effect to the above proposition. See Emmanuel Gaillard and Yas Banifatemi, ‘The Meaning of “and” in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process’ (2003) 18 ICSID Review.

<sup>737</sup>The criticism highlighted the factual differences including the difference in financial household burden, bearing of children and the social function arises from married couples which could cast a different view in the light of the granting of widowers pension sought for. See Cornides, ‘Three Case Studies on Anti-Discrimination’ (n 711) 5.



investment law as one which involves interaction of the national and international obligations urge the adaptation of sustainable standards that could stand in the system, namely the application of margin of appreciation, reasonableness and proportionality. This, according to Petersman would address the problem of intergovernmental regulation that infringes ‘democratic legitimacy, rule of law or fundamental rights.’<sup>738</sup>

The biggest lesson learnt from the ECHR is that we are able to see the effects of certain interpretations which are adopted by the Court. This research submits that the application of margin of appreciation, although may provide assistance in the determination of comparator, must not be adopted by international investment law as how it features in the ECHR. While the concept is useful, the application in the ECHR is too extensive. It is essential that deference is recognised but applied reasonably and proportionately. Proportionality must be given due importance in achieving this balance.

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<sup>738</sup> Petersman article suggested complimentary approach including multilevel constitutions, global administrative law and legal and constitutional pluralism. See Dupuy, Francioni, and Petersmann, *Human Rights in International Investment Law and Arbitration* (n 604) 40. For the inter-relation between the democratic rights of the people and investment arbitration, see Schneiderman, *Constitutionalizing Economic Globalization* (n 344).

## Chapter Six

### SYNTHESIS AND SUMMARY

#### 1.0 Introduction

The whole essence of legal comparative study is to see what lessons that could be derived from the experiences of other jurisprudences in answering similar questions. As studies in Chapters 3-5 has shown, there are threads of commonalities and differences between international investment law and the jurisprudences under comparison, namely GATT/WTO, EU and international human rights law. These commonalities and differences are essential to guide this thesis to establish an informed comparative outcome on the suitability of certain concepts or principles that can be applied in the interpretation of national treatment in international investment law.<sup>739</sup>

Although each chapter has tentatively indicated the useful apparatuses for likeness in the jurisprudences, this chapter will synthesise and operationalise them in the context of international investment law. This chapter will conclude the findings against the research questions put forth in the proposal. The first research question calls for a study on the emerging principles in national treatment in determination of likeness and legitimate regulatory interests.<sup>740</sup> This question is answered partly in Chapter Two which identifies the trend of the interpretation of national treatment across the

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<sup>739</sup>The assessment of the philosophies and contexts of the EU, GATT/ WTO and International Human Rights jurisprudences in Ch. 3-5 was attempted to arrive at a sound and informed comparison, a matter which is commonly criticised to be overlooked in functional comparative law approach. Michaels, 'The Functional Method of Comparative Law' (n 88); Whytock, 'Legal Origins, Functionalism, and the Future of Comparative Law' (n 88).

<sup>740</sup> See 4.1, Ch.1.

cases. Chapter Six particularly develops this observation to analyse the underlying value of national treatment. The methodology applied in achieving this is by doctrinal assessment of the national treatment provision under investment agreements and by comparative study with the GATT/WTO, EU and international human rights law. Chapter Six answers the most difficult part of the research question in suggesting and illustrating how decided investment cases could correspond with the underlying values of national treatment.<sup>741</sup>

The next important limb in the research question is to find out the relevance of GATT/WTO, EU and international human rights law in the interpretation of likeness and determination of legitimate regulatory measures.<sup>742</sup> This chapter extracts the lessons learnt from the jurisprudences and analyses its suitability and relevance to the investment cases, by evaluating and criticising where necessary the respective tribunals' approach in addressing the issues. This thesis concludes that the said jurisprudences are relevant and instructive to the issues in question.

At the end, this chapter provides a flowchart to suggest a systematic analysis of the criteria of likeness, the determination of legitimate regulatory measure and the interaction thereof, taking into account the lessons learnt from the relevant jurisprudences.

This chapter is executed under five main headings, namely, the value underlying national treatment, operationalisation of useful principles and methods in ascertaining likeness, reflection of the analytical framework, coherence and

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<sup>741</sup> See 4.1.3, Ch.1.

<sup>742</sup> See 4.2, Ch.1.

legitimate expectation and proposed criteria of likeness for national treatment in international investment law.

## **2.0 Lesson Learnt 1: The ‘Value’ Underlying National Treatment**

This section examines on how GATT/WTO, EU and the ECHR could assist national treatment in international investment law in understanding its own underlying values. The significance of this exercise is not only to identify the specific features of international investment law as compared to the other jurisprudences,<sup>743</sup> but it is also essential to answer the research questions on the doctrinal content of national treatment and the interaction of investment decisions to this underlying philosophy.

It is observed summarily that the non-discrimination principle in all the compared jurisprudences aim at prohibiting irrational government discriminatory measures. While this forms the commonality in this comparison, it must be acknowledged that this prohibition is also oriented to serve the jurisprudences’ specified purposes. The GATT/WTO aims for competition for the access in the market and liberalisation of trade, the EU quests for non-discrimination in the freedom to exercise capital movement and establishment, while international human rights law aims for equality in the exercise of fundamental right of property. The study of these jurisprudences’ linkage of its non-discrimination assessment to the philosophy of its treaties has provided the lenses to similarly measure the position of national treatment in investment treaties. This area has been an underdeveloped area in investment

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<sup>743</sup> Arguably, for a more acceptable functional comparative exercise. Michaels, ‘The Functional Method of Comparative Law’ (n 88).

decisions and scholarship which could have otherwise developed a ‘principled’ interpretation of national treatment.

Putting alongside the national treatment provision with the non-discrimination principles in the GATT/WTO, EU and the international human rights law, it surfaces what national treatment aims to achieve in international investment law. It enables us to see what it ‘is’ and ‘what it is not’ in comparison to the others. The relevant questions to be asked in this respect are basically: What is the value or underlying philosophy of national treatment in investment treaties? How could the interpretation of national treatment reflect these philosophies? The determination of likeness will benefit from this finding by making it as the operational and observational standpoint to construe the situations of the comparators. This is thus the first lesson learnt, i.e the need to search for the philosophy or underlying value of national treatment in international investment law.

In order to discern the philosophy of national treatment, one would have to understand its purpose and context. To put it simply, the national treatment provision is incorporated in the investment treaties to protect from discrimination. As opposed to general discrimination provisions, it is based on the nationality of the investment/investors which is the most needed protection by foreign investors in facing potential threats from the regulatory functions of the host state.<sup>744</sup> Thus by incorporating national treatment, it would in turn enhance the effectiveness of investment treaties in providing protection and promotion of investments. The relationship between national treatment and investment treaties indicates that national treatment comes

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<sup>744</sup> Federico Ortino mentioned that there is a difference between national treatment and most favoured nation treatment with the broad principle of equality. Nationality is the regulatory criterion in the former. See Ortino, *Basic Legal Instruments for the Liberalisation of Trade* (n 100) 122.

with a purpose which should be reflected in its interpretation. This includes the interpretation of likeness which is the most problematic part of the provision.

In attempting this issue, this thesis submits that the value of national treatment consists of two important values which are; ‘level playing field’ and ‘nationality based’ (or discrimination based on nationality). These values are potential to bring the operationalisation of the national treatment provision closer towards its objective and purpose.

These values are explained in the following subsections:

### *2.1 Level-Playing Field*

First and foremost, level –playing field corresponds with the purpose of national treatment. The very purpose of national treatment is to prohibit host states from treating less favourably foreign investors than that is accorded to local investors as part of the protection of investments. Investments will lose control of its profitability and economic efficiency with the interference of discriminatory measures by the government, the effect of which may push investments to inefficiency or inactivity. The interference of level playing field by government policies has triggered many investment cases. The US government via its Buy America measure in the *ADF Group Inc v US* case for instance has disrupted the level playing field between US and foreign (construction projects) and caused the claimant massive increase of cost to fabricate its steel at five different subcontracting facilities.<sup>745</sup> Similarly, in *SD Myers v Canada*, the level playing field between foreign and domestic PCB waste

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<sup>745</sup> *ADF Group Inc v USA*, (n 173), para 55.

remediation services was interfered by the ban on the export of PCBs to the detriment of the foreign investor including the loss of contracts and opportunities.<sup>746</sup> These interferences are considered as political risks, which are most worrying and often took investors by surprise outside the calculation of the ordinary course of business.<sup>747</sup>

It in turn upsets the legitimate expectations of foreign investors. The insertion of the national treatment clause and the signing of investment treaties are supposed to create a legal certainty that foreign and local investments will be treated alike and in a level playing field. In *CPI, Inc. v Mexico*, the tribunal acknowledged the legitimate expectation of foreign investors to invoke national treatment when the level playing field between competing investments is distorted. The tribunal asserted,

‘The fact that economic competitors have - and lobby for - different interests is not at all surprising. On the contrary, it is a fact of economic and political life which may be observed in any open society. Far from suggesting that they are not in like circumstances, it tends to suggest the opposite; it is precisely because they are in close competition that they lobby against each other - if they were not competing in the market for what are effectively interchangeable products, they would not trouble to maintain such lobbying activities. To accept Mexico's argument in all its breadth would be to neuter Article 1102, because it is precisely where the interests of foreign investors

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<sup>746</sup> *S.D. Myers Inc. v Canada*, (n 24), para 222.

<sup>747</sup> Discrimination by host states deprive investments from its value. See Noah Rubins and Stephan Kinsella, *International Investment, Political Risk and Dispute Resolution: A Practitioner's Guide* (n 424).

and domestic investors are in conflict that the principle of non-discrimination becomes most important.<sup>748</sup>

The case of *Mesa Power Group LLC v Canada* has featured an example of a last minute imposition of discriminatory measures by the government of Canada that was contrary to the initial set of expectations in the renewable energy sector. The claimant has brought up the issue of expectation, i.e Canada's failure to maintain a regulatory framework in conformity with its international obligations under NAFTA.<sup>749</sup> It is natural that an investor in such a sector would expect level playing field in the fair evaluation of projects and electrical grid access with other domestic and foreign investors.

In terms of interpretation of national treatment, the assessment of level playing field assists the tribunal to determine the angle of like situations between the comparators. This is possible by understanding what level playing field is the subject of the dispute which is affected by a regulatory measure. The correct approach is to construe level playing field in the competition of investment opportunities. By so doing, it raises 'economic standard' as the *tertium comparationis* to the interpretation of likeness.<sup>750</sup> This approach is sound to achieve a teleological and

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<sup>748</sup> *CPI, Inc. v Mexico*, (n 98), para 135.

<sup>749</sup> *MESA Power Group, LLC v Government of Canada* NAFTA, Notice of Intent to Submit a Claim to Arbitration under Section B of Chapter 11 of the North American Free Trade Agreement, 6 July 2011. See also Footer, 'On the Laws of Attraction: Examining the Relationship between Foreign Investment and International Trade' (n 318) 131.

<sup>750</sup> This standard has been applied in GATT/WTO and a number of investment cases (see the NAFTA cases mentioned above, in contrast to *Methanex v USA* and *UPS v Canada* which ignored the role of competition which is an economic standard in the determining of likeness). Diebold has highlighted 'economic standard' as one of the main approach in the interpretation of likeness in international economic law. See Nicolas F Diebold, 'Non-Discrimination and the Pillars of International Economic Law – Comparative Analysis and Building Coherency', *ILJ Emerging Scholar Paper 18 (2010)*. It is also interesting to relate the economic impact of discriminatory actions by states as highlighted by DiMascio and Pauwelyn that 'discrimination creates inefficiency.' The effect is well similar in



prudent interpretation of treaty, in assessing what is truly relevant to the text and context and by not over emphasising on the contrary.<sup>751</sup> This can at least reduce the dilemma in which tribunals face in considering whether the appropriate comparison is between like circumstanced investments (or investors), or like circumstanced treatment.<sup>752</sup> It can also alternatively assist the tribunal to take into account both approaches. For instance, in the case of *Methanex v USA*, the application of level playing field could have highlighted the effect of the regulatory measure on the competing businesses of methanol and ethanol producers. It will also on the contrary show that there is no relevance of comparison with the other methanol producer despite being more identical to the claimant because of the absence of the competitive relationship that would warrant level playing field.<sup>753</sup>

In the case of *CPI, Inc. v Mexico*, although the tribunal was persuaded to consider likeness of corn sweetener (HFCS) and sugar cane sweetener based on price regulation, the tribunal concluded that likeness in this case must be based on the subject of investments which are interchangeable and indistinguishable from the viewpoint of the end-users. The tribunal continued affirming that the regulation on

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investment terms. Although one may argue that the main role of investment treaties is not economic efficiency, it must also be noted that the protection of investors can only be meaningfully achieved if the investors could have full control of their investments' economic efficiency. DiMascio and Pauwelyn, 'Nondiscrimination in Trade and Investment Treaties' (n 49). See cases, *Methanex v USA*, (n 19) and *UPS v Canada*, (n 21).

<sup>751</sup> The tribunal in the case of *MHS v Malaysia* for instance has adopted a teleological approach in the interpretation of 'investment' by taking into account the context of economic development as set in the preamble of the investment treaty. See *Malaysian Historical Salvors Sdn, Bhd v. Government of Malaysia*, ICSID Case No. ARB/05/10, Award on Jurisdiction, 17 May 2007. Similarly, in the context of national treatment, the purpose of prohibiting states from discriminating foreign investments /investors has been to create a level playing field for the protection and promotion of investments as warranted the preambles of investment treaties. It is therefore absurd if the interpretation of likeness is taken linguistically and secluded from the context it belongs. Take for example the case of *UPS v Canada* where the tribunal ignored the competitive relation and the level playing field of the comparators in the same postal industry but peruse into any possible differences that could render the comparators unlike. See *UPS v Canada*, (n 21), paras 98-119.

<sup>752</sup> Bjorklund, 'National Treatment' (n 104) 39.

<sup>753</sup> *Methanex v USA*, (n 19).

HFCS is discriminatory when intended to protect producers of sugar.<sup>754</sup> This reasoning indicates implicitly that the tool ‘level playing field in the competition of investment opportunities’ was used to determine the angle of whether to choose likeness from the point of view of investment (or investors), treatment or other factors. Apparently, the regulatory regime designed to affect the price was not relevant to the question of likeness and applying so would negate the effect of the non-discrimination clause.<sup>755</sup>

In this aspect, the GATT/WTO provides guidance in what less favourable treatment means in understanding Article III.<sup>756</sup> Similar to Article III, the term ‘less favourable treatment’ in investment treaties is unqualified (except in like circumstances). It is also in line with the GATT Panel in the Section 337 case<sup>757</sup> which calls for effective equality of opportunities in respect of its establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.<sup>758</sup> The aim towards level playing field is reflected under the requirement of ‘directly competitive or substitutable products’ to establish likeness of products under the domain of Article III:2. In the *Appellate Body Report Japan- Taxes on Alcoholic Beverages*, the essence of level playing field was deliberated implicitly:

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<sup>754</sup> *CPI, Inc v Mexico*, (n 98), para 126.

<sup>755</sup> *Ibid.*

<sup>756</sup> One of the common cores of trade and investment is level economic playing field. See DiMascio and Pauwelyn, ‘Nondiscrimination in Trade and Investment Treaties’ (n 49); Vandevelde, *Bilateral Investment Treaties* (n 2) 337.

<sup>757</sup> United States-Section 337 of the Tariff Act of 1930, GATT Panel Report adopted 7 November 1989, BISD 36<sup>th</sup> Supp.345 (1990), para 5.11. This case was also quoted by the tribunal in the case of *CPI, Inc. v Mexico*, (n 98) para 111.

<sup>758</sup> See for instance Chile-US FTA 2003, < <http://www.ustr.gov/trade-agreements/free-trade-agreements/chile-fta/final-text>>, and Singapore-US FTA 2004, <[http://www.ustr.gov/sites/default/files/uploads/agreements/fta/singapore/asset\\_upload\\_file708\\_4036.pdf](http://www.ustr.gov/sites/default/files/uploads/agreements/fta/singapore/asset_upload_file708_4036.pdf)>, both accessed on 17 October 2013.

‘...Article III protects expectations not of any particular trade volume but rather of the equal competitive relationship between imported and domestic products.’<sup>759</sup>

‘In this case, the Panel emphasized the need to look not only at such matters as physical characteristics, common end-uses, and tariff classifications, but also at the "market place". 53 This seems appropriate. The GATT 1994 is a commercial agreement, and the WTO is concerned, after all, with markets. It does not seem inappropriate to look at competition in the relevant markets as one among a number of means of identifying the broader category of products that might be described as "directly competitive or substitutable".’<sup>760</sup>

The identification of competitive relationship as the angle of comparison indicated the likeness of the products from the viewpoint of the level playing field that exported products entitled to enjoy. Similar to GATT/WTO, investment treaties are also entered into as commercial agreements, if not public-commercial hybrid agreement. It is therefore similarly appropriate to construe the national treatment provision from the level playing field of the investors’ economic activities.

Level playing field in the assessment of non-discrimination principle is however not apparent in the EU context. The EU law, despite heavily grounded in an economic liberalised setting, is inclined in using its non-discrimination principle more towards prohibiting any restriction (which is discriminatory in nature) that would hinder its

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<sup>759</sup> Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, (n 387), p16. See also United States - Taxes on Petroleum and Certain Imported Substances, BISD 34S/136, para. 5.1.9.

<sup>760</sup> *Japan – Taxes on Alcoholic Beverages*, (n 387), p 25.

subjects from the enjoyment of the freedoms guaranteed.<sup>761</sup> The test in the EU jurisprudence is to ask whether the discriminatory treatment has resulted to restriction of freedom rather than the distortion of the level playing field with other investors. The EU law often invokes assessment of likeness under the purview of the Community principle of equal treatment.<sup>762</sup>

Similarly, the ECHR uses the non-discrimination principle to secure the enjoyment of the rights and freedoms set forth in the convention (in particular right to property) and thus does not in its jurisprudence construe the level playing field of the comparators.<sup>763</sup> The inclination in ECHR is to examine the situation of the comparators whether they are similar enough so as not to justify a differential treatment. Similarity and analogous situations seems to be the focal factor to enable the Courts to see whether there was less favourable treatment that would deny the claimant from the enjoyment of right to property.<sup>764</sup> Furthermore, in the ECHR jurisprudence, it promotes non-discrimination more towards ‘equality’ to ensure the rights are enjoyed equally without discrimination. In both EU and ECHR, the principle of non-discrimination is used to secure another legal right (freedom of establishment, free movement of capital and right to property), whereas in international investment law and GATT/WTO it is embedded in the protection itself. In the latter, the principle of national treatment therefore embodies a richer content to

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<sup>761</sup> The non-discrimination principle in the EU law is a ‘tool to pursue the goals of the Treaty: a safeguard of the free market and free competition. See Marco Gregg, ‘Revisiting “Schumacker”’: The Role of Limited Tax Liability in EU Law’, *Allocating Taxing Powers within the European Union* (Springer 2013) 45.

<sup>762</sup> See *Schumacker*, (n 488) and Case C-80/94, *Wielockx* [1995] ECR I-2493. See also Tracy A. Kaye, ‘Tax Discrimination: A Comparative Analysis of US and EU Approaches’ in Reuven S. Avi-Yonah, James R. Hines and Michael Lang (eds), *Comparative Fiscal Federalism: Comparing the European Court of Justice and the US Supreme Court’s Tax Jurisprudence*, vol 14 (Kluwer Law International 2007).

<sup>763</sup> Article 14 ECHR; see also Article 1 of Protocol 12 ECHR.

<sup>764</sup> *Case of Fredin v Sweden*, (n 666), para 60; *Marckx v. Belgium*, (n 640), para 32.

serve its own purpose and context which is to ensure level-playing field between nationals and non-nationals in the respective economic activities.

Another justification of preferring the concept of level-playing field over others such as ‘equality’ in the ECHR or ‘freedom’ in the EU law is that it has a more flexible stretch to accommodate likeness in truly fair situations. This will reflect the practical and real business atmosphere between local and foreign investors and allow the tribunal to decide a situation that is fair to both local and foreign investors in setting the platform for investment. Thus, it is useful to ensure that the national treatment principle is not advantageously benefitted possibly by the foreign investors which are already having competitive advantage over the local investors, or possibly by the host states by creating a false disadvantage to local investors. In the case of *El-Paso v Argentina*, the tribunal has taken into consideration the general impact of pesification on the banking sector as compared to the oil and gas sector which have benefitted from the export and the devaluation of peso. It is thus reasonable for the government to tax the unexpected profits as a way to rebalance the situation.<sup>765</sup> The measure may seem to be unequal but it is nevertheless fair and level. By applying the national treatment provision in the purview of what is level playing field enhances its role as supporting the rule of law in investment regime.<sup>766</sup> Correcting factual inequalities should not be regarded as discriminatory as it promotes fairness and

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<sup>765</sup> *El Paso v Argentina*, (n 173), para 314.

<sup>766</sup> The same concern was raised in an article which questioned the way some ECJ cases allowed the exploitation of the principle of equality and discrimination by claimants. The article highlighted in particular the cases of *Maruko*, *Römer* and *Test Achats* which took advantage of the difference of situations for particular gains. Cornides, ‘Three Case Studies on Anti-Discrimination’ (n 711). See also Case C-267/06, *Tadao Maruko v. Versorgungsanstalt der deutschen Bühnen* [2008] ECR I-01757; Case C-147/08, *Jürgen Römer v. Freie und Hansestadt Hamburg* ECJ (Grand Chamber) 10 May 2011 and *Test-Achats*, (n 724).

reasonableness. In a similar vein, the UNCTAD report of national treatment noted that,

‘However, where countries at different levels of development are parties to an IIA, such formal equality may disregard important differences in the actual situation and capabilities of the enterprises on each side. The formal “legal symmetry” of their legal situation may be accompanied by actual “economic asymmetry” (UNCTAD, 1999e). In such a context, application of the national treatment standard may require more than formal equality, so that the development needs of a developing country party to an IIA are taken into account in the definition and application of the standard.’<sup>767</sup>

The logic of level playing field allows reasonable justifications to take place if there is a need to correct the economic imbalance of the investment players. This would result to fair and sustainable application of national treatment both to the local and foreign investors.

Level playing field is also consistent with the general aim of investment treaties in ensuring a favourable investment climate and economic cooperation.<sup>768</sup> A favourable investment climate can only be achieved if there is competitive neutrality. The OECD, in noting the relevance of level playing field and competitive neutrality in achieving favourable investment conditions noted;

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<sup>767</sup> ‘National Treatment’ (n 151) 61.

<sup>768</sup> For instance in Article II of the Egypt - United States BIT (1986), it obliges both parties to ‘maintain a favourable environment for investments’ and recognises the importance of ‘economic cooperation’ in its preamble to foster bilateral trade and investment. Similarly, see Canada - Croatia BIT (1997) and Argentina - Germany BIT (1991).

‘The recommendation of level playing field is fully consistent with common definitions of competitive neutrality.’

This is due to the fact that once investments set in a host state, it has to abide by the local laws, including tax requirements which may be designed to disadvantageously affect foreign investors.<sup>769</sup> The essence of competitive neutrality is that no business entity is advantaged or disadvantaged because of its ownership.<sup>770</sup> A host state is considered to have violated competitive neutrality if its measures distort which nationality occupies particular investments. Competitive neutrality is especially needed to protect foreign investments against public sector business under government ownership (state owned enterprises).<sup>771</sup> An example of distortion of level playing field between a public sector business and a private investor is in the case of *UPS v Canada* where there was a clear exemptions of certain obligations (for instance payment of penalties, cost recoveries, cost of transition of systems), monopoly of certain custom functions and deprivation of advantages akin to brokerage service that was enjoyed by the Canada Post as a State enterprise.<sup>772</sup>

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<sup>769</sup> The role of competitive neutrality and level playing field will be even more needed in investment treaties that provide pre-establishment rights or freedom of establishment such the NAFTA, the German BITs the North American BITs and the ASEAN Comprehensive Investment Agreement. See Sandrock, ‘The Right of Foreign Investors to Access German Markets: The Meaning of Article 2(1) of the German Model Treaty for the Promotion and Protection of Foreign Investments’ (n 340).

<sup>770</sup> Antonio Capobianco, and Hans Christiansen, ‘Competitive Neutrality and State-Owned Enterprises: Challenges and Policy Options’ (OECD Publishing 2011) No. 1.; OECD, ‘The Multilateral Agreement on Investment Commentary to the Consolidated Text’ (n 188).

<sup>771</sup> This is the concern put forth by the OECD. Antonio Capobianco, and Hans Christiansen, ‘Competitive Neutrality and State-Owned Enterprises: Challenges and Policy Options’ (n 770)

<sup>772</sup> *UPS v Canada*, (n 21), para 97.

## *2.2 Nationality Based Discrimination*

This is a complex matter. The discussion of national treatment as a nationality based discrimination provision may not seem controversial at its surface, but its furtherance will involve the questions of intent, protectionist purpose and burden of proof. No matter how much the tribunal attempt to avoid or provide safe remarks on the relevance of (in particular) intent and protectionist purpose, they have to nevertheless deal with them in one way or another. National treatment as a nationality based discrimination will also impact on the determination of likeness especially when it is construed from the legitimacy of the regulatory measures in generally three situations—in the obvious presence of motivation to discriminate against a nationality, in the absence of such motivation and in the situation where other legitimate justifications exists.

This thesis submits that national treatment in investment treaties is nationality based and should be reflected in its interpretation. It suggests that, for a measure to breach national treatment there must be evidence that it was motivated by discrimination against foreign nationals than any other reason. This is based on a number of reasons. Firstly, the indication for a nationality based interpretation is explicitly and literally termed in the national treatment provision. The general construction of the provision obliges each party (a state) to an investment treaty to accord investors of another party (the national of another state) treatment no less favourable than it accords to investments of its own investors (the national of that state).<sup>773</sup> Nationality is thus the crux of this provision.

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<sup>773</sup> Such literal construction of the national treatment provision can be seen for instance in NAFTA Article 1102 (1) and (2).



Secondly, nationality-based assessment forms the contextual and purposive interpretation of national treatment. This does not only differentiate it to other applications of the non-discrimination principle in EU, ECHR or customary international law which are far more general in nature, it also confines its application to the correct beneficiaries of national treatment i.e to the foreign investors which are subjected to discrimination based on nationality rather than mere discrimination.<sup>774</sup>

Thirdly, nationality based assessment is inherent in many investment cases either directly or indirectly. The NAFTA cases for instance have considerably taken into account the nationality assessment in the alleged discriminatory measures. In *CPI Inc. v Mexico*, the tribunal asserted that:

‘When the clear impact of that discrimination falls on the foreign investor, the result is a violation of Article 1102 of the NAFTA’<sup>775</sup>

In *SD Myers, Inc v Canada*, targeting foreign nationals can be assessed by both intent and practical effect (treatment). Intent must be accompanied with practical effect.<sup>776</sup> In *GAMI*, the fact that the measure was not motivated by nationality but financial stability was the reason that it did not violate national treatment.<sup>777</sup>

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<sup>774</sup> This is particularly to note the approach taken by the tribunal in the case of *OEPC v Ecuador* which broadly expanded the scope of national treatment by subjecting a state to a breach of national treatment obligation even though it was done without the intent of discriminating foreign owned companies. See *OEPC v Ecuador*, (n 18), para 177.

<sup>775</sup> *CPI, Inc v Mexico*, (n 98), para 126.

<sup>776</sup> *SD Myers, Inc v Canada*, (n 24), para 252.

<sup>777</sup> This case was referred to by *CPI Inc v Mexico* to compare the nationality motivated measure and the reason to depart from the judgement. See *CPI Inc v Mexico*, (n 98), para 131.

Fourth, the existence of another general form of non-discrimination principle in some investment treaties urges the national treatment principle to be more concentrated on cases of discrimination based on nationality. The Romania-US BIT for instance prohibits contracting parties from ‘arbitrary or discriminatory measures’ in a separate provision from the national treatment provision.<sup>778</sup> The same provision could be found in the US-Argentina BIT.<sup>779</sup> It is observed that even in cases under these provisions, the tribunals were inclined to adopt the nationality based assessment. Two obvious examples under the abovementioned BITs are *Noble Ventures, Inc v Romania* and *LG&E v Argentina*.<sup>780</sup> In *Noble Ventures, Inc v. Romania*, the tribunal indicated the possibility of a case to succeed under the clause if there is discriminatory intent. The tribunal held,

‘But that in itself does not exclude the possibility that the proceedings constituted a discriminatory measure because it is possible for a single measure to be discriminatory if proof to that effect is given. As one cannot rely on objective criteria in such situations, the Claimant has to demonstrate that a certain measure was directed specifically against a certain investor by reason of his, her or its nationality.’

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<sup>778</sup> Romania-US BIT 1994, Article II(2)(b) and Article III(3).

<sup>779</sup> Article II (b), 1994 US-Argentina BIT.

<sup>780</sup> Both cases failed under this test. In *LG&E v Argentina*, the tribunal quoted *ELSI Elettronica Sicula SpA case (United States of America v. Italy)*, ICJ Report 1989 RLA 56 and required discriminatory treatment to fulfil three requirements, which are: an intentional treatment (ii) in favour of a national (iii) against a foreign investor, and (iv) that is not taken under similar circumstances against another national. As a note of comparison to the national treatment provision based on the two cases, this clause is perhaps resorted to when the claimant feels that there is possible evidence of intentional treatment but no clear comparator. See *LG&E Energy Corp. v Argentine Republic ICSID Case No. ARB/02/1, Decision on Liability*, 3 October 2006, para 146 and *Noble Ventures Inc. v. Romania*, (n 183), para 180.

In the case above, the tribunal did not find sufficient evidence that the measure was targeted on the claimant as a US company.<sup>781</sup> Such explicit assessment of nationality should often be exhibited in national treatment decisions. Cases such as *OEPC v Ecuador*, *UPS v Canada* and *Methanex v USA* have not incorporated the assessment of nationality motivated discrimination, indirectly conveying the messages that the national treatment provision could encompass a broad range of discrimination cases, and that the national treatment provision may not be able to prohibit measures motivated by discrimination against foreign national than any other reason despite being so apparent.

There is thus a need to pay attention to national treatment as a nationality based provision. There are several issues often related to this which are worth mentioned. First is its possible association with national treatment as an anti-protectionism principle and the requirement of intent. Both concerns have so far received no consensus in the acceptability and the application in investment disputes. This concern is understandable as in the finding of whether a particular national is targeted, evidences of protectionist purposes will pour in.<sup>782</sup> Secondly, it is argued by some commentators that by extending the interpretation as such, it will exceed its literal scope.<sup>783</sup> This is not required by the treaty.<sup>784</sup> Thirdly, it will cause difficulties/ hardship for the foreign investments to access government records.<sup>785</sup> Finally, it is also feared that it would equate the national treatment provision in

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<sup>781</sup> *Noble Ventures Inc. v. Romania*, (n 183), para 180.

<sup>782</sup> See *SD Myers, Inc v Canada*, (n 24), paras 161-195 on the allegations of protectionist statements 'in Canada by Canadians'.

<sup>783</sup> This is a general reluctance of investment tribunals to adopt a teleological approach, considering the new development of international investment law, the need to build the confidence therein and the manifest jurisdiction of arbitrators in the interpretation of the legal texts of the treaties.

<sup>784</sup> *Marvin Feldman v Mexico*, (n 15), para 181.

<sup>785</sup> In *Feldman v Mexico*, the tribunal mentioned; '[R]equiring a foreign investor to prove that discrimination is based on nationality could be an insurmountable burden to the Claimant, as thin formation may only be available to the government. [...]' See *ibid.* para 183.

investment treaties to that of GATT/WTO which has explicit purposive guide in Article III:1.

This subsequent discussion will address the issues one by one.

Nationality based discrimination inevitably encompasses the problem of protectionist intent. Tribunals have taken ambiguous views on this matter. In *SD Myers v Canada*, the tribunal states that,

‘Intent is important, but protectionist intent is not necessarily decisive on its own. The existence of an intent to favour nationals over non-nationals would not give rise to a breach of Chapter 1102 of the NAFTA if the measure in question were to produce no adverse effect on the non-national complainant.’<sup>786</sup>

This statement is also cited in the case of *Alpha Projektholding GmbH v. Ukraine* in emphasising the need of protectionist intent to be accompanied with more feasible evidence of discriminatory treatment.<sup>787</sup> There were also tribunals that unconvincingly refused to adopt this approach because of the absence of explicit language in the text but nevertheless acknowledged that investment treaties are designed to prevent discrimination based on nationality.<sup>788</sup> In line with this view, the tribunal in *Bayindir* upheld;

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<sup>786</sup> *SD Myers v Canada*, (n 24), para 254.

<sup>787</sup> *Alpha Projektholding GmbH v. Ukraine*, ICSID Case No. ARB/07/16, Award, 8 November 2010, para 427.

<sup>788</sup> *Feldman v Mexico*, (n 15), para 181.

‘If the requirement of a similar situation is met, the Tribunal must further inquire whether Bayindir was granted less favourable treatment than other investors. This raises the question whether the test is subjective or objective, i.e. whether an intent to discriminate is required or whether a showing of discrimination of an investor who happens to be a foreigner is sufficient. The Tribunal considers that the second solution is the correct one.’<sup>789</sup>

There must be a more rigorous assessment of nationality based motivation of a regulatory measure. This thesis submits however that the requirement is not the level of ‘intent’ but is grounded to a more assessable standard of ‘aim and effect’. While one would argue that an assessment of intent would be impossible and implausible, akin to that of an international criminal law assessment,<sup>790</sup> the assessment of aim and effect of nationality preference can be more achievable taking into account the circumstantial evidence of the dispute. If the tribunal is satisfied that the aim and effect of the regulatory measure is to discriminate against a particular nationality, the measure must be deemed illegitimate, unless if the host state could provide a legitimate justification. Protectionist purpose can be derived from the factual background of the case, its political drive (including lobbying), the design and the structure of the measure challenged. If there is such evidence, the host state will then has to provide reasonable justification for the legitimacy of the measure. This also addresses the third concern, in the sense that the burden of proof on the claimant is not as high as it would be to prove the requirement of intent. The

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<sup>789</sup> *Bayindir v Pakistan*, (n 290), para 390. See also *Thunderbird Case*, (n 199), para 177.

<sup>790</sup> Borzu Sabahi has pointed out the difference of assessing intent under objective responsibility of states in the International Law Commission’s Articles on Responsibility of States for Internationally Wrongful Acts in particular on the Genocide Convention that requires ‘intent to destroy’ as part of the definition of the crime. In contrast to this, the national treatment provisions do not incorporate such requirement and thus according to ILC, ‘it is only the act of State that matters, indecently of any intention’. See Sabahi, ‘National Treatment-Is Discriminatory Intent Relevant?’ (n 705).

claimant must show that the circumstances, the structure of the measure and the effects thereof is nationally motivated and affected.

As far as the next argument is concerned, by taking into account the context of national treatment and the rigorous examination of the ‘circumstances’ as in the like circumstances requirement, it does not render exceeding its literal scope. It is in line with the rule of interpretation in Articles 30-31 of the Vienna Convention. Methodologically, it is inappropriate to stick to the literal meaning of likeness and ignoring the interpretation of ‘circumstances’. The assessment of circumstances allows the tribunal examine relevant facts and the national treatment contextually. Similarly, strictly adhering to the three prong test without taking into account the need to move beyond has proven inappropriate. It could lead to either ‘false likeness of circumstances’ which would cause host states a hard time to justify the measures, or ‘false failure of like circumstances’ which would allow host states to escape from the burden of justifying the measure especially when the weakness of such justification is expected. In *OEPC v Ecuador* for instance, there was no active assessment on whether the measure was targeting particular nationals, leading us to the understanding that a simple situation of less favourable treatment can be accepted by any national against any domestic investor.<sup>791</sup> As there was no finding of ‘targeting foreign investor or singling out foreign investor’, the assessment of like circumstances evolved around a broad net that encompasses a foreign investment in the oil exploration sector against domestic investors of various sectors. This is a false likeness of circumstances. Consequently, the host state is unexpectedly left to justify

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<sup>791</sup> Similarly, it was upheld in the case of *Bayindir v Pakistan* that the showing of discrimination of an investor who happened to be a foreigner is sufficient. See *Bayindir. v. Pakistan*, (n 290), para 390.

the discriminatory allegation on broad grounds akin to ordinary discrimination cases. Ultimately, the interpretation of national treatment defeats its purpose.

The GATT/WTO is instructive in this aspect, contrary to the fear of the trade and investment equation in the fourth argument above. Although the aims and effects test receives a mixed response in the realm of GATT/WTO, it could nevertheless potentially provide guidance to international investment law as it requires the search of protectionist purpose and the disproportionate discriminatory impact on foreign investors.<sup>792</sup> The GATT/WTO is grounded on the basis of curbing protectionism. It is explicitly stated in Articles III that regulations should not be applied to imported or domestic products ‘so as to afford protection to domestic production’. It is this explicit guide that led to the GATT panel decision in *United States: Taxes on Automobiles* to uphold the classifications of autos based on the gasoline consumptions as not like products because there was a bona fide aim of regulation and the effect was not inherently protective.<sup>793</sup>

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<sup>792</sup> There was a shift of approach in GATT to adopt the aims and effects test in 1992-1995. It was put aside later but it seems that this principle has re-emerged in the year 2000 in the case of *Chile – Taxes on Alcoholic Beverages*. The Appellate Body stated that,

‘we consider that a measure’s purposes, objectively manifested in the design, architecture and structure of the measure, are intensely pertinent to the task of evaluating whether or not that measure is applied so as to afford protection to domestic production.’

See *Chile – Taxes on Alcoholic Beverages*, para. 71, WT/DS87/AB/R, (adopted Jan. 12, 2000), para 71.

<sup>793</sup> The test was contested in particular in the case of *Japan-Alcoholic Beverages*. The rejection of the aim and effect test according to Hudec was not conclusive. There is correctness in this approach to some certain extent, including ‘protective application’ and ‘discriminatory purpose’ that seemed to be applied, yet discreetly in subsequent cases such as *Bananas Panel Report*, *Canadian Periodicals and Hormones Case*. See Hudec’s article E. Hudec, ‘GATT/WTO Constraints on National Regulation: Requiem for an “Aim and Effects” Test’ (n 123) See also Appellate Body Report, *European Communities –Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591; Appellate Body Report, *Canada –Certain Measures Concerning Periodicals*, WT/DS31/AB/R, adopted 30 July 1997, DSR1997:I, 449 and Panel Report, and *EC Measures Concerning Meat and Meat Products (Hormones)*, Complaint by the United States, WT/DS26/R/USA, adopted 13 February 1998, as modified by Appellate Body Report WT/DS26/AB/R, WT/DS48/AB/R, DSR1998:III, 699.

There is no comparable provision that form a purposive guide for national treatment in the international investment treaties. Nevertheless, it does not require a complex assessment to realise that investment treaties similarly prohibit protectionism as the basis of government regulatory measures. This can be deduced from the similar political economy of trade and investment and the use of the national treatment as a traditional international economic law cornerstone concept in most liberalising trade and investment treaties.<sup>794</sup>

This thesis submits and acknowledges however that while protectionism is the subject of discipline under the national treatment provision, protectionism is not totally illegitimate. The tribunal in the case of *SD Myers, Inc. v Canada* seemed to support that protectionist purpose can be legitimate. In *SD Myers, Inc. v Canada*, the protectionist purpose was to ensure the economic strength of the Canadian industry to maintain the ability to process PCB within Canada in the future.<sup>795</sup> The tribunal stated:

‘The indirect motive was understandable but the method contravened Canada’s commitment under NAFTA’.

There is logic behind excusing certain acts of protectionism if it is genuinely for the public need or national security. This is not an alarming reduction of application of national treatment, but would on the contrary be in line with the general principles of

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<sup>794</sup> This line of argument is in line with Kurtz’s proposition that the quest for state purpose in a national treatment inquiry could enhance the role of the national treatment provision as a discipline to constrain protectionism. See Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’ (n 102).

<sup>795</sup> *SD Myers Inc. v Canada*, (n 24), para 255.



reasonableness, good faith and public interest.<sup>796</sup> It must also be noted that the best approach to follow is whenever there is evidence of protectionism, the burden of proof will be higher on the host state to justify the rational and proportionality of the measure. As in the case of *SD Myers v Canada*, although its protectionist measure was somewhat approved by the tribunal, the host state has failed to defend it under the ground of proportionality. Thus protectionism is prohibited and should be curbed only if there is no reasonable justification that legitimises it.

It is thus submitted that construing national treatment provision as a tool that is grounded on nationality and anti –protectionism (notwithstanding recognising the possible exceptions) has a role in interpreting the provision. It does not only lead a way for a meaningful and effective provision (in protecting the ‘right thing’ for the investors and not protecting just ‘anything’), it also solves significantly the interpretative hurdle of the national treatment provision.

An example of a lack of protectionist purpose enquiry can be seen in the case of *OEPC v Ecuador*. The tribunal applied a mere discrimination test and did not construe the relevance of protectionist enquiry. The result was that likeness was held across the economic sectors. There was no protectionist purpose, but there was still a breach of national treatment. This is an unfair construction of national treatment, because states, in particular, would be caught in surprise as the assessment of likeness by the tribunal could stretch anywhere, as in this case, from oil exploration to flowers and banana producers. The correct disciplining on states’ behaviour, if one were to use the word, must only be that the investment treaties could only

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<sup>796</sup> This is where margin of appreciation will play its role, together with the principle of proportionality. Please refer 3.3.1 for an analysis on margin of appreciation.

‘discipline’ a state if it has crippled a level playing field condition of foreign and domestic investors because of protectionism (protecting the latter), not coupled with legitimate reason. This is what states understand, or rather what should derive from the incorporation of a national treatment provision in an international investment treaty.<sup>797</sup>

Another example is the case of *Grand River Enterprises Six Nations, Ltd., et al. v. United States of America*. Had the purposive enquiry took place, it would have analysed the relevant facts of the case, inter alia; the growth of the claimant’s market share with other NPMs share of the US market as a result of substantial reduction of PM sales and market share; and the regulatory response to that i.e the implementation of a complementary legislation in 2002 (known as the contraband law) that prohibited tax stamps on cigarettes for NPM and to eventually forfeit cigarettes without them. The involvement of the participating members and the state to the contraband law, the reasonableness of the measure allegedly motivated by public health and the discriminatory effect on the foreign investor may be indicative to the finding of protectionism with no concrete justification.<sup>798</sup>

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<sup>797</sup> This is in line with the ‘effect and purpose’ method proposed by one scholarly writing claiming that the motivation to discriminate because of difference in nationality is essential for a breach of Article 1102. This could avoid a declaration of breach without protectionist intent. See Rojas, ‘The Notion of Discrimination in Article 1102 of NAFTA’ (n 107), New York, <<http://centers.law.nyu.edu/jeanmonnet/archive/papers/05/050501.pdf>> accessed on 29 July 2013.

<sup>798</sup> The arguments in this case did not go to the direction of discussing purposive protectionism either by the claimant or the respondent (except in a passing, see *Grand River Enterprises Six Nations, Ltd., et al. v. United States of America*, UNCITRAL/NAFTA, Award, 12 January 2011, para 171). The claimant was perhaps under the impression that it would be easier to proceed with the ‘broad and remedial fashion’ argument as in *OEPC v Ecuador* (see (n 18), para 161). Unlike *OEPC v Ecuador*, one could argue that the facts in the *Grand River* case have stronger evidence of purposeful protectionism. This submits that if the aim and effect test is applied, as opposed to the strict requirement of intent, it would have made it possible for the claimant to challenge the reasonableness of the regulatory measure against the background of protectionist circumstances. This would also affect the plausibility of the ‘like legal circumstances’ employed by the tribunal based on the exact chain of contested regulation. See *Grand River Case*, (n 798) paras 165-166.

Taking into consideration protectionist traits is important. States could otherwise hide behind self-serving legitimate objectives of health or environment while actually systematically advantage its domestic investments. Particularly when there is lobbying involved, it is hard to tell whether the public policy justification is a bona fide one and not one which is representing an interest group.

Had the aims and effect test was applied in *Methanex v USA*, it could have also revealed the effect of the discriminatory measure on the methanol producer and a strong protectionist purpose of the measure. Although eventually the result of the case could be the same (by upholding the environment measure), in terms of burden of proof, the state would have to show a really strong reason why the environment measure is up and above the obvious protectionist effect.

A lesson learnt in this aspect is to understand the position of protectionism, or operationally, the search of protectionist measures in international investment. This is an essential aspect of the interpretation of national treatment that must be given attention to. As seen in the above discussions, it plays a purposive role to ensure that the essence of the national treatment provision is met, as a provision that prohibits discrimination based on nationality.

### **3.0 Lesson Learnt 2: Principles and Methodologies in Assessing Likeness**

Comparison with the GATT/WTO, EU law and International Human Rights has enabled the evaluation of methodological strengths and shortcomings in the application of the principle of non-discrimination. This section will highlight the

important principles and methodologies observed from the GATT/WTO, EU law and International Human Rights Law and their relevance to the interpretation of likeness in international investment treaties.

### *3.1 Lessons from GATT/WTO*

As seen from the GATT/WTO jurisprudence, the main tests of likeness are the traditional characteristics test, aims and effects test and competitiveness and substitutability test. This part will attempt to apply the competition test as the most useful test of the three as a potential criterion of likeness in investment cases. As for the aims and effects test, it is more useful in forming the ground context of national treatment, hence, a significant part of its role is taken as an instructive guide in enhancing or emphasising national treatment as a nationality based provision. Therefore, this section will highlight the importance of aim of effect test only to the extent that it may be useful in assessing likeness.

#### *3.1.1 Competition Test*

Competition is the most obvious indicator of likeness especially the market or service based investments. This is due to the dependency of the investments of this type on the proceeds from consumers based on the performance in the competitive market. This would determine the rates of returns and the financial viability of the investments. When there is a regulatory measure that provides competitive advantages to a particular investment to the deprivation of other investments which share the same consumers, the measure has arguably undermined the level playing field of investments in like situations.

One could not deny the inter-relatedness between trade and investment, that production of goods is one of the core activities of investments (apart from services).<sup>799</sup> One could also argue that the purpose of product based investments is to produce in the very market place as an alternative to export. If the latter is chosen as the method of business, the relevant jurisprudence would otherwise be the GATT/WTO. Thus an investment in this line could be affected by measures that affect the customers of a particular investment and the competition test should become helpful as how it is helpful in the GATT/WTO context.

However, (as discussed in Chapter Three) when investment cases containing competing investments were brought to the tribunal under national treatment, there were mixed views on the acceptance of the competition test, or rather the acceptance of GATT/WTO in which competition test is an important evaluation. It was controversially ignored in earlier cases of *Methanex v USA* and *UPS v Canada*. Although it has eventually found its way in the decision of *CPI Inc. v Mexico*, the competition test was not articulated in many other investment decisions and remain a subject of debate.<sup>800</sup>

The tribunal in the case of *Methanex v USA* has rejected the competition test in favour of the search of ‘most like circumstances’. This led to a narrow reading of national treatment. The claimant alleged the MTBE ban was affecting the sale of methanol as every ethanol sale took away a sale of methanol. The claimant put forth

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<sup>799</sup> For the inter-relation between trade and investments, see e.g. Footer, ‘On the Laws of Attraction: Examining the Relationship between Foreign Investment and International Trade’ (n 318); DiMascio and Pauwelyn, ‘Nondiscrimination in Trade and Investment Treaties’ (n 49).

<sup>800</sup> In the same vein, Kurtz highlighted the deficiency of the tribunals in addressing the relevance of the competition test in the cases. See Kurtz, ‘The Merits and Limits of Comparativism: National Treatment in International Investment Law and the WTO’ (n 102) 256.

that Methanex and other methanol producers are in like circumstances with US domestic ethanol producers. The difference of approach on the question of likeness arose where Methanex claimed that the competition test should be applied, while the US government insisted on the ‘most like circumstances approach’ considering that there were other domestic methanol producers.<sup>801</sup> The tribunal held that methanol and ethanol producers are not in like circumstances despite the fact that both were producing oxygenate and competing the same consumers. Although it may be challenging to decide such case in the presence of another most like investor producing methanol, the tribunal should gear likeness to the likeness of circumstances as warranted in investment treaties even if it may mean to conclude likeness to a lesser characteristically or physically like investment. The point is, in the given set of facts in the case, both oxygenate producers are similar enough without dwelling into the scientific differences which are not relevant in the context of invocation of the national treatment protection. In relation to this, it brings us to the realisation that there are situations where most like investors may not be in competition with the claimant as compared to a less like investor which is adequately alike enough in the absence of the former.

As in the case of *Methanex v USA*, methanol and ethanol producers as oxygenate producers and competitors should be considered as alike despite its scientific differences. The tribunal rejected the relevance of GATT/WTO and upheld that Article 1102 should be read in its own terms.<sup>802</sup> The tribunal did not however

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<sup>801</sup> *Methanex v USA*, (n 19) , para 16.

<sup>802</sup> The tribunal asserted,

‘International law directs this Tribunal, first and foremost, to the text; here, the text and the drafters’ intentions, which it manifests, show that trade provisions were not to be transported to investment provisions. Accordingly, the Tribunal holds that Article 1102 is to be read on

elaborate what those own terms were. It seemed that the tribunal rejected the ‘competitiveness approach’ together with its rejection of the relevance of GATT/WTO jurisprudence. By indication, the ‘own terms’ include an acceptance of detailed assessment of characteristics of the products (in this case the methanol and ethanol) exactly as one would expect in a comparison of likeness in GATT/WTO characteristic test. This is not only a backward/ traditional method even in the GATT/WTO as compared to the competition test, it is also not suitable to be applied in the investment context as it denies the situation of the investments which is the crucial aspect of determination of likeness. This effect may not come to the attention of the tribunal during the assessment, but a calculation of the result of the decision has revealed an awkward outcome. The outcome is that investments which are competing, in the same economic sector are not in like circumstances to contrast with the case of *OEPC v Ecuador* that have allowed a broad range of investments as comparators. This case has contributed to the incoherence of national treatment.<sup>803</sup>

With regards to comparison based on the physical attributes or characteristics (in the context of article III:2 GATT), is described by Hudec as ‘sterile’ and having ‘no purpose oriented’ in the determination of important regulatory issues like national treatment.<sup>804</sup>

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its own terms and not as if the words “any like, directly competitive or substitutable goods” appeared in it.’

See *Methanex v USA*, (n 19), para 37.

<sup>803</sup> In relation to this, there are commentaries and critics on the future of NAFTA Chapter 11, one of it includes a prediction that it will ‘dampen the enthusiasm to launch future investment arbitrations’. It further stated that ‘future claimants will have to prove that they are truly in “like circumstances” to a domestic industry to qualify under Chapter 11. An investor that is indirectly affected but that is not in precisely the same competitive category will be out of luck. See Lawrence Herman, ‘Trade Law Memo-Volume 4 Issue 5- The Methanex Case and the Future of NAFTA Chapter 11’ <[http://www.casselsbrock.com/CBNewsletter/Trade\\_Law\\_Memo\\_Volume\\_4\\_Issue\\_5\\_The\\_Methanex\\_Case\\_And\\_The\\_Future\\_Of\\_NAFTA\\_Chapter\\_11](http://www.casselsbrock.com/CBNewsletter/Trade_Law_Memo_Volume_4_Issue_5_The_Methanex_Case_And_The_Future_Of_NAFTA_Chapter_11)> accessed 15 April 2013., at <[http://www.casselsbrock.com/CBNewsletter/Trade\\_Law\\_Memo\\_Volume\\_4\\_Issue\\_5\\_The\\_Methanex\\_Case\\_And\\_The\\_Future\\_Of\\_NAFTA\\_Chapter\\_11](http://www.casselsbrock.com/CBNewsletter/Trade_Law_Memo_Volume_4_Issue_5_The_Methanex_Case_And_The_Future_Of_NAFTA_Chapter_11)>, accessed on 15<sup>th</sup> April 2013.

<sup>804</sup> E. Hudec, ‘GATT/WTO Constraints on National Regulation: Requiem for an “Aim and Effects” Test’ (n 123).

‘Most like circumstances’ is not plausible an approach. The first reason is that it could lead the tribunals to construe likeness restrictively. As in the case of *Methanex v USA*, the tribunal has ignored the competitive situation that Methanex had to face with the ethanol producers, which are considered by the tribunal as less similar investments. Ethanol producers could have qualified as alike in the absence of the other methanol producers which are ‘in most like circumstances’ as coined in the case.<sup>805</sup> Secondly, this approach would result to governments hiding behind most similar situated domestic investments (possibly being created by the government) with exactly similar characteristics to potential foreign investments which are the targets of discriminatory action.

The message is unclear. In the case where there is no identical comparator, will the ethanol competitor be still considered unlike to methanol producers? It is submitted that likeness could not be relatively construed based on the existence or absence of an identical or most like comparator. Likeness of a situation is alike when it is by its own merits alike. If the investors in the *Methanex* case are compared with based on their own merits, i.e by way of its competitive situation, then perhaps it would not after all, as the terms used by the tribunal, be of ‘forced application’ to ignore identical comparators.<sup>806</sup>

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<sup>805</sup> Andrew Newcombe has also highlighted this possibility, ‘that the appropriate comparator group might not be the domestic investment in identical circumstances, but another competitor in like circumstances’. See Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 2) 169.

<sup>806</sup> The tribunal referred to the case of *Pope & Talbot v Canada* on like circumstances. The tribunal remarked,

‘It would be a forced application of Article 1102 if a tribunal were to ignore the identical comparator and to try to lever in an, at best, approximate (and arguably inappropriate) comparator.’

See *Methanex v USA*, (n 19), Part IV-Chapter B, para 19. See also *Pope & Talbot Inc v Canada*, (n 20).



Similarly, in the case of *UPS v Canada*, the tribunal aimlessly construed the differences of two strikingly similar investments in the postal services whilst neglecting the importance of its competitive relationship. Cass criticised this approach saying:

‘National treatment protection would be dramatically reduced under that approach, as it would eliminate any right to protection whenever there were differences between the complaining party and the compared investment or investor even if those differences were slight enough to affect the competitive relationship that Article 1102 was designed to protect’.<sup>807</sup>

The competitive relationship between UPS Canada and Canada Post including similar times for delivery, similar service features and similar customers, should be enough to show likeness. Any justification otherwise must be one that is substantial and relevant to the matters at issue. One needs only to look at the differences of treatment alleged by the claimant (which includes denial of brokerage service, exclusion of certain custom functions and the obligation to pay certain costs related to CADEX) to realise that the more it has shown the similarity of affairs UPS and Canada Post are involved in. The justifications brought forth in this case were on the exact reasons it brought for unlikeness, which could lead one to draw an inference that there was actually no legitimate justifications that the case could resort to if it fails under the likeness test. At this point, the differences accepted by the tribunal

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<sup>807</sup> *UPS Inc. v Canada*, (n 21), para 14.

(which are different objects, mandates and transports, deliver goods in different ways) seem superficial and irrelevant.<sup>808</sup>

It would be impossible to request for identical characteristics in investments. There must be differences in one way or another.<sup>809</sup> Here, what is relevant is to measure likeness on the point of the level playing field the investors seek in the protection of national treatment, and there could be no better assessment than the competition of the investments in a given market when such evidence is available.

Thus, the competition approach is the most instructive interpretation that international investment disputes could learn from the GATT/WTO jurisprudence. The GATT/WTO jurisprudence has adopted the competition test despite the availability of tangible characteristics of products that is relatively easier to be examined. This can be seen in *Australia—Subsidy on Ammonium Sulfate*<sup>810</sup> and *European Community—Measures on Animal Feed Proteins*.<sup>811</sup> It could provide the relevant range of ‘accordion of likeness’, by broadening the narrow approach as in *Methanex v USA*, *UPS v Canada* and *Feldman v Mexico* (where strict characteristic assessment was employed) and narrowing a broader approach as in *OEPC v Ecuador*.

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<sup>808</sup> Taking identical twins as an analogy, it is inappropriate to give similar fitness test when one is physically weaker or medically inferior to another. Upon comparison, the physical strength of the twins should be taken into account to examine likeness for a level playing field rather than insignificant characteristic based factors such as the location of a mole, birthmark or hobby.

<sup>809</sup> In the case of *CPI v Mexico* the tribunal acknowledged that differences can be construed in many possible angles. The important criteria is one which is most relevant to the object and purpose of national treatment. The tribunal mentioned, ‘ Any other interpretation would negate the effect of the non-discrimination clauses, because it would always be possible to find differences between the way competing products are owned, managed, regulated or priced.’ See *CPI Inc. v Mexico*, (n 98), para 126.

<sup>810</sup> BISD, vol.2, 188 (1952).

<sup>811</sup> BISD, 25<sup>th</sup> Supp.49 (1979). Hudec described *Australia—Subsidy on Ammonium Sulfate*<sup>811</sup> and *European Community—Measures on Animal Feed Proteins* cases as containing meaningful discussions of ‘like product’ as they considered the competitiveness of physically dissimilar products. See E. Hudec, “‘Like Product’: The Differences in Meaning in GATT Articles I and III’ (n 123).

The *Methanex* tribunal made this following remark when commenting on the relevance of GATT/WTO:

‘Hence, the Tribunal begins with an inquiry into the plain and natural meaning of the text of Article 1102. Paragraphs 1, 2, and 3 of Article 1102 enjoin each Party to accord to investors or investments of another Party “treatment no less favorable than that it accords, in like circumstances, to its investors [or investments]. . .”. These provisions do not use the term of art in international trade law, “like products”, which appears in and plays a critical role in the application of GATT Article III. Indeed, the term “like products” appears nowhere in NAFTA Chapter 11.’<sup>812</sup>

What the tribunal failed to understand is that the ‘product’ in this case was the exact investment that suffered less favourable treatment. The tribunal also failed to understand that competition is a neutral test, which is not specific for GATT/WTO. It is able to cast similarity of situations which is relevant in trade and investment and would be highly relevant in the context of national treatment.

The tribunal should acknowledge competitive relationship in fulfilling the essence of the claim of national treatment even though the breach of national treatment is upheld. There may be cases of tight business competition but no scientific differences to tell them apart. What is not addressed is the role of competition which could cast a different and sensible view of likeness of situations towards reasoned

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<sup>812</sup> *Methanex v USA*, (n 19), para 29.

awards in the international investment jurisprudence. In this aspect of assessment, GATT/WTO could highly cast guidance in the interpretation of national treatment.

### 3.1.2 Aims and Effect Test

In the context of GATT/WTO, the aims and effect test was revolutionary when it was first introduced for deviating from the traditional characteristics test of like products. This may be understandable as products are traditionally defined by their tangible features, end uses and consumer preferences. Furthermore, there is Article XX GATT to take the hurdle of assessing the legitimacy of the challenged regulatory measures.

The proponents of the aims and effects test argue that the traditional or literal way of construing likeness could in some cases result to a ‘no purpose-oriented criteria’ and ‘would fail to prohibit some product distinctions that should be prohibited and prohibit some product distinctions that should not be prohibited’.<sup>813</sup> The aims and effect test is applied to tell the adverse effects of the absence of a *bona fide* purpose

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<sup>813</sup> See for instance in the case of *Malt Beverages*, where the panel took into account the purpose of the provision. The panel noted:

The purpose of Article III is thus not to prevent contracting parties from using their fiscal and regulatory powers for purposes other than to afford protection to domestic production. Specifically, the purpose of Article III is not to prevent contracting parties from differentiating between different product categories for policy purposes unrelated to the protection of domestic production. The Panel considered that the limited purpose of Article III has to be taken into account in interpreting the term "like products" in this Article.

Similarly in the *Auto-Taxes* case which applied the aim and effect test, the panel found that the product distinctions between automobiles were *bona fide* and that the effect was not protective. This decision was however not adopted. See United States-Measures Affecting Alcoholic and Malt Beverages, June 19, 1992, GATT B.I.S.D (DS23/R - 39S/206), para 5.25; United States: Taxes on Automobiles, 11 October 1994, WT/DS31/R (unadopted); Chile-Taxes on Alcoholic Beverages, 12 January 2000, WT/DS87/AB/R. See also United E. Hudec, ‘GATT/WTO Constraints on National Regulation: Requiem for an “Aim and Effects” Test’ (n 54).

to differentiate products based on a certain criteria. Because criteria can be made, it is therefore plausible to examine the rational of those criteria.<sup>814</sup>

The relevance of aims and effects test in the context of likeness is that it allows consideration of the legislative purpose.<sup>815</sup> This is an instructive guide for investment cases. If a measure is introduced, say environment standards, and resulted to two otherwise similar investments unlike, the aims and effect test would then do the checking of whether the environment standards are not only reasonable or rational on its merits, but whether in the whole context has targeted a particular investment based on nationality. If there is no justification and if there is effects on a particular foreign investor, then it could be adversely concluded that the measure was of no grounds other than protecting the local investment. Therefore, the measure that is the determinant factor of the differences between the investments could not be valid.

This test should be applied in the case of *Methanex v USA* to examine whether the environmental objective was the main aim of the measure which can be adversely indicated from the structure, effects and protective application of the measure weighing against proportionality and its least restrictive application on foreign

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<sup>814</sup> In *Malt Beverages* case, the US was unable to rationalize the different tax rates imposed on the type of grape which grows only in the south eastern of United States and the Mediterranean region. The panel concluded that failure to be indicative of purposeful protectionism of local producers. The tax thus could not hold differences between what are otherwise like products. See United States-Measures Affecting Alcoholic and Malt Beverages, June 19, 1992, GATT B.I.S.D (DS23/R - 39S/206), para 5.23-5.26.

<sup>815</sup> Aims and effect test has been discussed in GATT in generally a few aspects, likeness and less favourable treatment. The demarcation line is however unclear. Roughly, up to the point of determining the legitimacy of the regulatory measure and its application as a criteria that differentiate the investments of an otherwise similar situation, it is relevant to the assessment of likeness. Where the discussion expands on assessing the disproportionate effect on the foreign investors, it leans more towards answering the question of less favourable treatment.

investments.<sup>816</sup> It was not so in this case. The tribunal was occupied in the examination of the differences of physical properties of ethanol and methanol and the relevance of the most like investor in the market. This is exactly a no purpose-oriented criteria as described by Hudec and resulted to the failure to prohibit investment distinctions when it should be prohibited. The tribunal has ignored two important assessments which are the relevance of competition and the purpose of the regulation.<sup>817</sup> The assessment of aims and effect test would have resulted to a different decision.

Similarly in the case of *Grand River Enterprises Six Nations, Ltd., et al. v. United States of America*, the claimant urged to be compared as a non-participating manufacturer (NPM) with no exemption to its escrow payment under the Allocable share amendment off-reservation sales to the Subsequent Participating Manufacturers (SPM). The SPMs do not make MSA payments with respect to their pre-MSA share.<sup>818</sup> The tribunal refused to consider the competitive situation and protectionist threat faced by the claimant and preferred an identical / characteristic approach of likeness. According to the tribunal, the comparators should be other firms engaged in the wholesale distribution of cigarettes in the US and potentially subject to enforcement actions under the state's complementary legislation.

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<sup>816</sup> The claimant in the case of *Methanex* has forwarded that USA must satisfy whether the measure was necessary to fulfill the environmental objective, proportionate, least restrictive on foreign investments and do not constitute a disguised restriction on foreign investments. These factors were not construed by the tribunal in the likeness stage, and would presumably be dealt with after likeness is established as it adopted the three – pronged assessment of likeness. This observation is discussed in 3.3.2 below. See *Methanex v USA*, (n 19), para 9 Part IV- Chapter B.

<sup>817</sup> The aims and effects test is appropriate rather as an alternative argument after the competition test. The competition should at first instance rules likeness between the methanol and ethanol producers. The assessment of the legitimacy of the measure would follow in the next step, applying the three prong test. Alternatively, the appropriateness of the regulatory measure must be taken into account for a sound examination of likeness.

<sup>818</sup> Master Settlement Agreements (MSA).

On the flipside of the same argument, the aim and effect test could save governments from accidental discriminatory effects on foreign investors which are not based on protectionism. In such circumstances, the unlikeness of a situation because of a bona fide non-protectionist measure will avoid host states from breach of national treatment because of random discriminatory effects.<sup>819</sup> An obvious example of this is the case of *OEPC v Ecuador* which lacked the assessment of the protective aim and discriminatory impact of the challenged measure. The government of Ecuador nevertheless was held to have breached the national treatment obligation solely on the ground of discriminatory impact without due regards to the justifications and absence of protectionist aim. Here the justification of the states on the reasonableness of a regulatory measure is important. The tribunal may validate or invalidate a regulatory distinction based on its adverse inference on the reasonableness and proportionality of the measure.<sup>820</sup>

One may argue that since national treatment in international investment treaties are mostly not accompanied with an explicit and restrictive exception clause as Article XX in GATT/WTO, the aims and effect test becomes more relevant.<sup>821</sup> This is even more so especially when the merge justification approach of construing likeness is

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<sup>819</sup> Hudec's view may be instructive in the quest for protectionist aim. He suggested the use of 'protective application' by reflecting the decision of the Appellate Body in *Alcoholic Beverages* which mentions that '...protective application can most often be discerned from the design, architecture and the revealing structures of a measure.' Appellate Body Report on *Alcoholic Beverages* WT/DS8/R, WT/DS10/R, WTDS11/R (July 11, 1996), at 18.E. Hudec, 'GATT/WTO Constraints on National Regulation: Requiem for an "Aim and Effects" Test' (n 123).

<sup>820</sup> This issue is discussed under deference (under margin of appreciation below). This means that the aims and effects test provides more regulatory autonomy to the host states. In the context of GATT/WTO, see Michael Ming Du, 'The Rise of National Regulatory Autonomy in the GATT/WTO Regime' (2011) 14 *Journal of International Economic Law* 639, 658.

<sup>821</sup> As exceptions to this, see the Article 24 (2)(b) of the 1994 Energy Charter Treaty, Article 17 of the 2009 ASEAN Comprehensive Investment Agreement (ACIA) and the Association of Southeast Asian Nations and Comprehensive Economic Cooperation with Korea and China (AKIA and ACHIA). See discussions on Article XX GATT/WTO and international investment treaties in Legum and Petculescu, 'GATT Article XX and International Investment Law' (n 319); Céline Lévesque, 'The Inclusion of GATT Article XX Exceptions in IIAs – A Potentially Risky Policy' (n 450) .

adopted.<sup>822</sup> The opened structure of the national treatment in investment treaties allows regulatory measures to be assessed in either stage of interpretation, either in the likeness stage or the justification stage. It also opens the tribunal to the flexibility of determining legitimacy of a measure of various grounds, considering that investments are of many forms and complexity.

The absence of Article XX GATT/WTO resemblance in investment treaties is undoubtedly a reason for a more active and wider assessment of the justifications of a regulatory measure.<sup>823</sup> The inclusion of Article XX GATT/WO resemblance on the other hand would open the risk of restricting the tribunals from determining justifications which are outside the exception list. Furthermore, it would result to a mere formalistic assessment of exception and would not allow the merge justification test to occur in the determination of likeness. It is submitted that whether or not the exceptions to the investment treaties are included, it should not cast a significant difference in the investment regime that should itself embody and recognise the public elements involving sovereigns, environment and the people.<sup>824</sup>

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<sup>822</sup> In GATT/WTO, the finding of bona fide regulation will become redundant with Article XX which comes after the construction of likeness as it also requires the same finding. This research suggests that merge of justification test is to be adopted in certain situations. See 'Practicality of the Three Prong Test of National Treatment in the Determination of Comparators' in 3.3.2 below.

<sup>823</sup> To the contrary, one may argue that the inclusion of the Article XX GATT/WTO provision in investment treaties is to provide flexibility in the exceptions. See discussion on the matter in Andrew Newcombe, 'General Exceptions in International Investment Agreements' [2008] BIICL Eighth Annual WTO Conference <[http://www.biicl.org/files/3866\\_andrew\\_newcombe.pdf](http://www.biicl.org/files/3866_andrew_newcombe.pdf)> accessed 15 July 2013., <[http://www.biicl.org/files/3866\\_andrew\\_newcombe.pdf](http://www.biicl.org/files/3866_andrew_newcombe.pdf)>, accessed on 13 July 2013.

<sup>824</sup> *Ibid.*



## 3.2 *Lessons from the EU Jurisprudence*

### 3.2.1 *Emphasis on the ‘situation’ of the comparators*

The EU cases in respect of freedom of establishment and free movement of capital have highlighted the examination of situations of the comparators. In examining the situation of the comparators, both the factual and legal situations of the comparators are taken into consideration.

The assessment of situation does not require a total similarity or a hundred per cent similarity. It is adequate if the comparators can show that they are similarly situated for the purpose of a discrimination claim. Hence in the cases of *Schumacker*, the court held likeness based on the overall tax situation of the taxpayer and the positions in both the home and host state, although as a rule, residents and non-residents are non-comparable.<sup>825</sup> The assessment of similarity can overrule even the most established principle, if it is within the court’s view that it is unreasonable and discriminatory.<sup>826</sup> Although this exercise was motivated by the search for equality in taxes and the right of freedom of establishment, it provides a useful apparatus in which investment tribunals should consider in assessing likeness.

In the investment context, the situations of the investors should be examined based on its overall factual and legal situations. The overall factual situation will capture the discriminatory impact of measure, protectionism and competitive relationship that may exist between the comparators. This could provide the tribunal with useful

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<sup>825</sup> *Schumacker*, (n 488), para 37.

<sup>826</sup> In the case of *Schumacker*, the court looked at the overall tax situation of the taxpayer and the positions in both the home and host state. *Ibid.*, para 31, 37.

assessment in the angle in which likeness should be construed. An illustration of this would be as in the case of *Grand River Enterprises Six Nations, Ltd., et al. v. United States of America* where the tribunal construed likeness to confine investments under the same legal requirement. The tribunal asserted that the correct comparator should be other firms in the wholesale distribution business and subject to the same enforcement actions under the complementary regulation. The tribunal quoted various investment cases that supported this line of approach:

‘While each case involved its own facts, tribunals have assigned important weight to "like legal requirements" in determining whether there were "like circumstances." The *ADF* tribunal thus emphasized that both the claimant and its U.S. competitors were subject to the same U.S. "Buy America" provisions. *Pope & Talbot* found that the relevant comparators were lumber exporters subject to the same restrictive legal regime as the claimant, so there was no denial of national treatment if exporters in other unregulated provinces were not so limited. *Feldman v. Mexico* found the relevant comparators for purposes of MFN analysis to be a limited group of cigarette exporters subject to the same legal requirements as the claimant. The *Methanex* tribunal (citing *Pope & Talbot*) emphasized the importance of assuring that purported comparators face similar regulatory requirements. Looking at the question from the other direction, *UPS v. Canada* found a key difference between the parties there to be that Canada Post was subject to legal requirements under national law and international postal agreements that did not affect UPS.’

The tribunal however did not construe the factual situation of the claimant which could have revealed the competitive situation of the claimant and the disparate disadvantage that the measure has caused to Grand River as compared to the Subsequent Participating Manufacturers (SPM) who were the US cigarette manufacturers. The SPM did not have to make MSA payments with respect to their pre-MSA market share. The difference in treatment has caused the cigarettes by Grand River to be deprived from tax stamp and consequently declared forfeited. The tribunal should have constructed a purposive reading of national treatment by looking at all relevant facts of the case, especially where there are protectionist purpose and competition involved. Even the cases quoted by the tribunal in the passage above have somewhat construed a narrow assessment of likeness, i.e by looking at the legal situation of the comparators.

While legal requirements are possible to be ‘deliberately created legal situation’, the factual circumstances is more realistic and could highlight the genuine situations of likeness. This could be the economic parameters of likeness that includes the competitive relationship between the investors. The tribunal must be able to mark the line of which situation that should be correctly looked at in a particular situation.<sup>827</sup>

This would also cast a difference in the judgment of the *UPS v Canada* case in investment arbitration. The situation that the investor was in – similar needs of certain treatments relating to the postal industry which were enjoyed by the local comparator – was ignored by the tribunal. Rather than construing the situation of the investor, the tribunal took a literal approach of comparing likeness based on

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<sup>827</sup> Diebold, *Non-Discrimination in International Trade in Services* (n 376).

characteristics of the investments which diverted the decision away from the meaning of national treatment.

### 3.2.2 *Effet Utile*

The EU approach in reminding the *effet utile* of the EU integration in discrimination cases is a useful guide. It provides a firm direction for the court to determine whether a measure is discriminatory and restrictive to its achievement of the enjoyment of fundamental freedoms. The benefits of the *effet utile* approach are inter alia, that it could lead an incomplete rule effective, curbs the attempt to limit protection by literal interpretations and focusses on the function of a concept.<sup>828</sup> In the minimalistic nature of the national treatment provision, this principle could assist in finding and apply the essence of national treatment.

Generally, the two components of the underlying philosophies as explained in 2.1 and 2.2 above, namely ‘level playing field’ and ‘nationality based’ form the *effet utile* of national treatment. The aim of the treaties is to provide level playing field to foreign investors /investments against nationals.

In application, it will avoid narrow interpretations of a particular limb in the provision in the seclusion of the context. The cases of *Methanex v USA*, *ADF Group Inc v US* and *UPS v Canada* are a few obvious examples of non-construction of the broader context of national treatment in the analysis. In the case of *Methanex* for instance, the tribunal may be carrying on (of what it perceived correct), an

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<sup>828</sup> Norbert Reich, *Understanding EU Law: Objectives, Principles and Methods of Community Law* (Intersentia nv 2005) 31.

assessment of likeness by requiring the most like investment, but an *effet utile* approach would instruct the tribunal to look beyond the material assessment of likeness to likeness of the circumstances in enjoying the economic level playing field between foreign and nationals as guaranteed by the investment treaties.

Similarly in the *ADF Group Inc v US*, the nationality based regulation was not highlighted as an important criterion of assessment of the legitimacy of the regulatory measure that resulted to a non-level playing field of nationals and foreign investors.

In the case of *UPS v Canada*, the legitimacy of the regulatory measure was not construed at all, as the national treatment decision halted at the narrow interpretation of likeness which did not take into account the obvious interference of level playing field between competing investments.

The *effet utile* principle is different from the treaty object and purpose approach. One may argue that if the approach of interpretation is solely based on the aims of the investment treaties, it would result to a pro-investor interpretation.<sup>829</sup> The preambles of the investment treaties are clearly favouring foreign investors and would significantly affect the regulatory space of the host states. This thesis suggests that the *effet utile* of national treatment must include the general principles of reasonableness and proportionality. These elements combined would form a holistic and balanced approach in national treatment. It is a step towards a teleological

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<sup>829</sup> J Romesh Weeramantry, *Treaty Interpretation in Investment Arbitration* (Oxford University Press, USA 2012). , Christoph Schreuer, 'International Investment Law and General International Law – From Clinical Isolation to Systemic Integration?' <[http://www.univie.ac.at/intlaw/wordpress/pdf/comments\\_treaty\\_interpret.pdf](http://www.univie.ac.at/intlaw/wordpress/pdf/comments_treaty_interpret.pdf)>, accessed on 13 July 2013.

interpretation of national treatment which enhances legitimacy and effectiveness of the treaty.<sup>830</sup> This is in line with Article 31-33 of the Vienna Convention on the Law of Treaties (VCLT) which requires observance of good faith, ordinary meaning and context.

An interesting note to make when discussing *effet utile* is its possible application in investment agreements which have bigger economic integration objectives.<sup>831</sup> The ASEAN Comprehensive Investment Agreement (ACIA) for instance aims at achieving ASEAN Economic Community (AEC).<sup>832</sup> Looking at the composition of the provisions, one would conclude that it resembles the EU economic integration (freedom of establishment etc.). The question is, is it possible that the interpretation of national treatment will also follow the approach by the EU? It must be noted that the economic integration in the EU forms a strong *effet utile* in the interpretation of the non-discrimination principle in the freedoms guaranteed. If that is the case, host states must then be ready to accept the significant reduction of regulatory space, both in the assessment of justification of the regulatory measure both at the comparability level or the justification level.

On the other hand, there are specific features of the ACIA that could possibly turn the interpretation approach away from the EU law. The effect of a particular paragraph in the preamble that urges the member states to recognise ‘the different levels of development within ASEAN especially the least developed Member States which require some flexibility including special and differential treatment’ is

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<sup>830</sup> Teleological methodology of interpretation would mark the maturity of the international investment law. See DiMascio and Pauwelyn, ‘Nondiscrimination in Trade and Investment Treaties’ (n 49).

<sup>831</sup> This discussion is first introduced in Ch.4 of this thesis.

<sup>832</sup> ACIA 2009, (n 471), Preamble.

untested. This is a unique feature of the ACIA and could be a strong pushing ground for member states to justify differential treatment or unlikeness of two otherwise similar investments.

The *effet utile* must therefore be tailored to the aim of the treaty, and therefore, although it may be tempting to follow the EU approach in achieving economic integration, regards must be made to the intrinsic features of the treaty.<sup>833</sup> In investment agreements such as ASEAN, it will be interesting to see how the national regulatory interest is balanced or tolerated in the furtherance of the economic integration. In this particular situation, the invocation of the principles of good faith, reasonableness and proportionality are of prime importance. Applying the *effet utile* approach, the tribunal is able to look both within and beyond a particular limb of the national treatment provision to capture interpretation according to the VCLT.<sup>834</sup>

The advantage of the application of *effet-utile* is that it revives reference to the context of the jurisprudence in the examination of discrimination. Taking into account the *effet-utile* of the investment treaties purpose is a plausible approach as it strives to give meaning to the text. In the case of *Noble Ventures v Romania*, the tribunal noted that:

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<sup>833</sup> ASEAN integration has been criticised for its lack of political will as compared to the EU. See Tan, 'Will ASEAN Economic Integration Progress Beyond a Free Trade Area?' (n 516).

<sup>834</sup> In a similar vein, Schreuer has highlighted the connotations related to the restrictive and effective interpretation of investment treaties, the former being sided to the host state while the latter to the investors. He cited the case of *Mondev International v United States* which disregarded such approaches of interpretation, but promoting interpretation in accordance to the VCLT. The tribunal in *Mondev* held:

43. In the Tribunal's view, there is no principle either of extensive or restrictive interpretation of jurisdictional provisions in treaties. In the end the question is what the relevant provisions mean, interpreted in accordance with the applicable rules of interpretation of treaties.

See *Mondev International v. United States of America*, (n 64); Schreuer, 'International Investment Law and General International Law – From Clinical Isolation to Systemic Integration?' (n 829).

‘Reference should also be made to the principle of effectiveness (*effet utile*), which too, plays an important role in interpreting treaties.’<sup>835</sup>

Walde linked the principle of effectiveness to ‘good faith’ in Article 31 of the Vienna Convention of the Law of Treaties, although having a tenuous relationship, it nevertheless gives due recognition to the ‘sacred text’ – in that every element has to have some sense.<sup>836</sup> In the case of *Urbaser S.A. and Consorcio de Aguas Bilbao Biskaia, Bilbao Biskaia Ur Partzuergoa v. Argentine Republic* the tribunal stated,

‘When considering the purpose either of the BIT as a whole or of a particular provision, the Tribunal has to give such purpose an understanding that comports with the equally important principle of effectiveness (or principle of *effet utile*). Any treaty rule is to be interpreted in respect of its purpose as a rule with an effective meaning rather than as a rule having no meaning and effect. This principle is one of the main features of the law of treaties and has been applied by many ICSID Tribunals. It is given effect within Article 31(1) of the Vienna Convention by virtue of the requirement to interpret in good faith. Effectiveness of a treaty rule denotes the need to avoid an interpretation which leads to either an impossibility or absurdity or empties the provision of any legal effects.’<sup>837</sup>

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<sup>835</sup> *Noble Ventures Inc. v. Romania*, (n 183), para 50.

<sup>836</sup> Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ (n 539) 739. Lauterpacht marked a stronger relationship between the principle of effectiveness and good faith. He contended that ‘the principle of effectiveness constitutes a general principle of law and a cogent requirement of good faith’. H Lauterpacht, ‘Restrictive Interpretation and the Principle of Effectiveness in the Interpretation of Treaties’ (1949) 26 *British Year Book of International Law* 48, 83.

<sup>837</sup> *Urbaser S.A. and Consorcio de Aguas Bilbao Biskaia, Bilbao Biskaia Ur Partzuergoa v. Argentine Republic*, ICSID Case No. ARB/07/26, Decision on Jurisdiction, 19 December 2012, para 50, 107.



It is also related to the ‘purposive’ approach in the context of Article 31 (1) VCLT.<sup>838</sup> The purpose is not only referred to the purpose or function of the treaty, it could also be referred to the purpose and function of a particular concept or principle in the treaty.<sup>839</sup> This is an important tool needed in the interpretation of national treatment which has its own purpose and function (as a nationality – based discrimination provision), the application of which would add a meaningful substance to the interpretation of national treatment.

The *effet-utile* of international investment law, i.e ‘promotion and protection of investments’ is under-developed and less linked to national treatment.<sup>840</sup> Based on the existing development of the jurisprudence, it is unclear on the extent of protection intended in the investment treaties. It is deemed that protection would be delivered by way of the separate substantive provisions of expropriation, fair and equitable treatment (FET), national treatment, most favoured nation treatment (MFN) and full protection and security but the notion of investment protection by itself is not adequately articulated across the provisions. Thus, it is not surprising that in the national treatment interpretation, it is sometimes seen that the scrutiny of likeness was taken too far that the context or aim of national treatment and the *effet-utile* of the investment treaty is neglected. An illustration of this is the case of *UPS Inc. v Canada* where the scrutiny of the comparability of UPS and Canada Post was

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<sup>838</sup> Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ (n 539) 739,758–765. For concise discussion on *effet utile* and the non-codified rules of interpretation in the context of investment treaties, refer Weeramantry, *Treaty Interpretation in Investment Arbitration* (n 829) 143–194.

<sup>839</sup> Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ (n 539) 764.

<sup>840</sup> The importance of investment protection as catalyst in the assessment of national treatment is the reason why it is chosen as the analytical framework of this research, together with the concept of reasonableness. These two concepts are introduced in Ch.1 and explained further in the context of national treatment in investment law in Ch.2.

too deep into its characteristics that it out shadowed other considerations of circumstances reflecting the need of protection by the investor. In *UPS v Canada*, the tribunal noted that ‘that the importation of goods by courier required different customs treatments because of their different characteristics’.<sup>841</sup> This approach was criticised in the Separate Statement that by placing the orientation of finding likeness by asking ‘are the circumstances unlike?’ It is an advantage to the host state and will not lead the tribunal to the justification of the treatment no matter how discriminatory it is.<sup>842</sup> The context of national treatment in providing protection for foreign investors against discriminatory actions from the host state will be defeated. By placing the *effet utile* importantly,<sup>843</sup> it will at least bring about three emphases in the investment treaty interpretation, firstly, that attention will not divert to small scrutiny of characteristics of likeness, secondly, that priority will be given to the circumstances of the investors as the prime factor for comparison and thirdly, that it will enhance the application of proportionality and reasonableness of a measure in the light of the *effet-utile* of the investment treaties.

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<sup>841</sup> *UPS v Canada*, (n 21), para 99.

<sup>842</sup> *UPS v Canada*, Separate Statement of Dean Ronald A. Cass, 24 May 2007 (n 206), page 19.

<sup>843</sup> The *effet utile* of the national treatment will be explained in Ch.6. It is generally a holistic principle which should incorporate the values that national treatment provisions are nationality based discrimination provisions and that they function to provide level playing field for the protection and promotion of investment and recognise the public role of the state as long as they are executed reasonably, proportionately and in good faith.

### 3.3 Lessons from the International Human Rights Law

#### 3.3.1 Margin of Appreciation

Investment cases have not been explicit in the application of margin of appreciation in approving comparability of investors. It has nevertheless been considered implicitly. For instance in the case of *El-Paso v Argentina*, the issue was whether the banking sector which are mainly Argentinians and the oil and gas sector companies which are mainly foreign-owned are in like circumstances in facing the pesification measure. The tribunal accepted the government's measure as reasonable; i.e to balance for each sector the advantages and disadvantages of the general economic situation.<sup>844</sup> In the case of *Feldman* for instance, when the claimant alleged discrimination for the denial of rebate which was given to other investors in the tobacco industry, the tribunal upheld the domestic rationales of treating producers and resellers differently. The tribunal held:

‘As discussed in the Article 1110 section (supra, paras.115, 129), there are at least some rational bases for treating producers and re-sellers differently, e.g., better control over tax revenues, discourage smuggling, protect intellectual property rights, and prohibit gray market sales, even if some of these may be anti-competitive. Thus, as discussed in the expropriation section, the Tribunal does not believe that such producer – reseller discrimination is a violation of international law.’<sup>845</sup>

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<sup>844</sup> *El Paso v Argentina* (n 173), para 310.

<sup>845</sup> *Feldman v Mexico*, (n 15), para 170.

In another case of *Paushok v Mongolia*, the tribunal accepted the host states justification of the difference of tax law imposed on gold and copper as against the other industries such as the petroleum sector, and between gold and copper itself mainly to avoid tax evasion in the gold mining industry and to use the proceeds of copper exports for the advancement of copper production.<sup>846</sup> The tribunal has been explicit in not interfering in the wisdom of the justification made by the host state in the absence of a strong claim of discrimination by the claimant of the measure being ‘abusive’ and ‘irrational’.<sup>847</sup>

However, in the case of *OEPC v Ecuador*, margin of appreciation was not given to the host state. Despite the host state’s argument that the VAT refund policy was to ensure that the competition condition is not changed within an economic sector, the tribunal ruled that the claimant which was in the oil sector to be in like circumstances with other exporters of flowers, mining and seafood. Likeness was construed based on the criteria of ‘exporters’ rather than producers, manufacturers or exporters based on the economic sectors which would serve the purpose of the VAT.

Thus, as can be seen in *OEPC v Ecuador* it is observed that without giving deference or margin of appreciation to the host states, the interest of the host state (which includes the interest of the people) would not receive the attention it deserves especially if the tribunal do not rigorously assess the objectivity and reasonableness of the measure. The recognition of the state’s interest in property is less emphasised in investment cases as a principle. If the state’s interest is recognised by way of

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<sup>846</sup> *Sergei Paushok, CJSC Golden East Company, CJSC Vostokneftegaz Company v The Government of Mongolia* UNCITRAL, Award on Jurisdiction and Liability, 28 April 2011, para 316.

<sup>847</sup> *Ibid.*

margin of appreciation, it would potentially yield a more practical outcome which takes into account democratic legitimacy<sup>848</sup> and evolutive interpretation.<sup>849</sup>

The practical on-going of state administration must be taken into account. While it is expected that the states should grant full application of the protection of properties under the treaties, the administration of states could not have intended to give away legislative autonomy in all aspects especially when there is legitimate public need.

There are at least a number of reasons why margin of appreciation should be applied in the interpretation of national treatment:

1. *Sustainable Jurisprudence*: The application of margin of appreciation helps the development of a sustainable jurisprudence. It allows the states to comply and meet the standards of the international treaties and in line with the changing needs, norms or ‘shift of value’ of the society.<sup>850</sup> It tolerates the states’ need to regulate and help to create the legitimate expectation of the foreign investors in matters within the margin of appreciation of the states, particularly relating to likeness of circumstances.
2. *Reducing Clashes and Enhance Legitimate Expectation*: Especially in the view that international treaties are becoming closer and connected to each

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<sup>848</sup> Yourow, *The Margin Appreciation Doctrine in the Dynamics of European Human Rights* (n 686) 75

<sup>849</sup> *Ibid.*, 108.

<sup>850</sup> In the context of ECHR, such flexibility is needed in borderline cases in which it is hard to determine discriminatory treatment when there is certain shift of values in the society. Ellie Palmer, *Judicial Review, Socio-economic Rights and the Human Rights Act* (Hart Publishing 2009) 287.

other,<sup>851</sup> the doctrine of margin of appreciation could help in reducing clashes and enhance the legitimate expectation of the standard of protection in investor/ individual- states claims. The incoherence would leave one to expect a different award or compensation arising out from a single regulatory measure brought under two different regimes, which would at the end makes the whole international regime a world of speculation.<sup>852</sup> The margin of appreciation is described a ‘teleological and dynamic interpretative techniques’ that contributes to the effectiveness of the system.<sup>853</sup>

### 3. *Wide Coverage of Investment and Absence of Exhaustive List of Exceptions:*

The wide coverage of investment may be affected by the states regulation. Regulations can affect from almost all aspect of investments. Especially in sensitive areas of investments which involve public amenities which are privatised such as water sewage and electricity, government measures may be largely felt by foreign investors. This nature makes the doctrine of margin

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<sup>851</sup> States within a region may have or will enter into regional international human rights treaties and at the same time having commitments under various investment treaties. For instance the European countries having the ECHR commitments, BITs and the EU law as well as the (upcoming) American FTAA which may be colliding with the ACHR. Schill made a remark on the ability of states to comply with investment obligations by way of deference:

‘At the same time, it is important that States do not feel unduly prejudiced by the system of international investment protection and continue to be able to both accept arbitration as a legitimate way for settling investment disputes and remain able to implement legitimate domestic public policies.’

See Stephan Schill, ‘Rethinking the Substantive Standards of Protection Under Investment Treaties – How Much Deference Should Investment Treaty Tribunals Pay to the Regulatory or Judicial Acts of Host States?’ in The International Bureau of the Permanent Court of Arbitration (ed), *Flaws and Presumptions: Rethinking Arbitration Law and Practice in a new Arbitral Seat: Mauritius International Arbitration Conference 2010* (Mauritius Government Printing Office 2012) 365.

<sup>852</sup> As hypothetically speculated of the outcome of *Metalclad*, due to the ECHR probable invocation of ‘control of use of property’, there would be no compensation if it was to be brought under ECHR. See Freeman, ‘Regulatory Expropriation under NAFTA Chapter 11’ (n 615). On a real speculation, it could be seen from the case of *Bernardus Henricus Funnekotter and Others v. Zimbabwe*, (n 619) under ICSID and *Mike Campbell (Pvt) Ltd and Others v. Zimbabwe*, (n 619) invoking human rights protection under SADC. See discussion on the overlapping of human rights and investment claims in Ch.5. See *Metalclad Corporation v The United Mexican States*, ICSID Case No. ARB (AF)/97/1, 30 August 2000.

<sup>853</sup> Rhona KM Smith, *Textbook on International Human Rights* (3rd Edition, Oxford University Press 2007) 90.

of appreciation necessary, similar to the ECHR which has wide coverage of claims.<sup>854</sup> Furthermore, international investment treaties does not have explicit list of exceptions as one would find in Article XX GATT/WTO which is due to the nature of trade.<sup>855</sup> Thus the doctrine of margin of appreciation could soften the effects of the investment treaties on the states, which could be otherwise too harsh on the exercise of regulatory function.

4. *Practical Tool of Administrative Law*: Margin of appreciation is the tradition of European countries to balance conflicting rights in public law. For the purpose of administration, as states have ‘direct and continuous contact with the vital forces of their countries’, they are seen apt to assess the local needs.<sup>856</sup> It reflects a democratic standard (together with reasonableness and proportionality) that can harmonise and reconcile the interest of the investors and the people. As proposed by Walde, this judicial importation of democratic standards could be elevated as one of ‘comparative administrative law’ as general principles of law under Article 38 (1)(c) of the ICJ Statute or as a principle of interpretation deriving from ‘restrictive interpretation’ in the past.<sup>857</sup>

5. *Consistency with General International Law Practice*: Margin of appreciation is not only applied in domestic laws. While it is renowned in the

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<sup>854</sup> This observation is also made by Freya Baeten in drawing the similarities between international human rights and international investment law. This research provides how this observation could be advanced, i.e by the application of margin of appreciation in assessing likeness. See Freya Baetens, ‘Discrimination on the Basis of Nationality: Determining Likeness in Human Rights and Investment Law’ (n 97).

<sup>855</sup> There are exceptions in some investment treaties. See discussion on Aims and Effect Test in 3.1.2 above.

<sup>856</sup> *UK v Connors*, para 82. See also Palmer, *Judicial Review, Socio-economic Rights and the Human Rights Act* (n 850) 182.

<sup>857</sup> Walde, ‘Interpreting Investment Treaties: Experiences and Examples’ (n 539).

ECHR, it is also considered as a norm of interpretation in the form of deference in ECJ, WTO and ICJ.<sup>858</sup>

6. *State Concerns in Investor-State Disputes*: Eventually, the existence of proper guideline on how to construe likeness will not be left under the risk of ‘who arbitrates’.<sup>859</sup> This stems from the concern that many arbitrators are from the commercial field or the industry who would have the tendency to construe the government and investors in a level playing field, thus construing the cases from a commercial point of view and disregard, neglect or overlook governments as a sovereign power which decisions would impact the people of the government. The doctrine of margin of appreciation would place proper regards to the societal needs and values which are state concerns.

The application of margin of appreciation must however be guided primarily by other principles of reasonableness, proportionality and good faith. The downside of the ECHR jurisprudence in this aspect is the lack of these elements portrayed in its case law despite its resonances as fundamental principles.<sup>860</sup> The investment jurisprudence must take cognisance this experience in the ECHR and the impacts that lack of proportionality would bring to the legitimacy of investment decisions.<sup>861</sup>

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<sup>858</sup> Shany, ‘Toward a General Margin of Appreciation Doctrine in International Law?’ (n 715).

<sup>859</sup> Another problem that may arise from this is the tendency of commercial arbitrators to ignore general public international law which is more rooted on the nature of states as sovereigns and public interest.

<sup>860</sup> For explanation and illustration on this matter, please refer to Ch.5.

<sup>861</sup> The legitimacy of investment treaties are subject to comments by observers, among which concerns are the imbalance of states obligations against the absence of explicit countervailing duties by the investors and the fast track investor-state dispute arbitration. See Luke Eric Peterson, ‘Evaluating Canada’s 2004 Model Foreign Investment Protection Agreement in Light of Civil Society Concerns’ [2006] Canadian Council for International Co-operation (CCIC). <[http://www.ccic.ca/files/en/what\\_we\\_do/trade\\_2006-06\\_foreign\\_investment\\_memo\\_e.pdf](http://www.ccic.ca/files/en/what_we_do/trade_2006-06_foreign_investment_memo_e.pdf)>.



The importance of proportionality is recognised in cases. In the case of *Parkerings v Lithuania*, the tribunal held, that a discriminatory measure can only violate international law if it is ‘unreasonable or lacking proportionality, for instance, it must be inapposite or excessive to achieve an otherwise legitimate objective of the State’.<sup>862</sup> In that case, the tribunal accorded to the public interest justification brought by the host state in justifying the difference of treatment between the comparators.

### *3.3.2 Practicality of the Three Prong Test of National Treatment in the Determination of Comparators*

In investment arbitration cases, there are at least two factors of why likeness is construed from the viewpoint of the regulatory measure or justification. Firstly, it is due to the scarcity of like comparators (ranging from identical to most like to like comparators in terms of the nature of investment) and secondly due to the vulnerability of investments as they are prone to be effected by government regulations from every aspect of investment (not confined to pricing as in most GATT/WTO cases) including employment, compliance with environment, health and safety regulations and economic implications.

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accessed on 20 July 2013. Other concerns are, in the context of NAFTA the ‘democratic deficit’ of law making and investment arbitrations as a ‘private for a for public issues’. Jeffery Atik, ‘Repenser NAFTA Chapter 11: A Catalogue of Legitimacy Critiques’ (2003) 29 Loyola-LA Public Law Research Paper.

<sup>862</sup> *Parkerings v Lithuania*, (n 257), para. 368.

The factors mentioned have somehow supported the practicality of this approach. When there are other investors which are in the same economic sector or in competition but not discriminated by the measure, the tribunal would put its attention to them. When there is none, then there would be a tendency that the comparator is sought from other investors that share similar circumstances in view of the legislation imposed. Andrew Newcombe has put forth a hypothesis in this aspect, that the relevant comparator in response to a legislative measure on pollution would appropriately be an investor in the same area although the investor may be in a different economic sector as compared to an investor in the same economic sector but located in another area in which is not affected by the legislation.<sup>863</sup>

### *The Balance*

As the ECHR jurisprudence has indicated, over-construing likeness from the regulatory measure may not lead to appropriate results. An example of a case that over-construed likeness from the regulatory measure in investment arbitration is the *OEPC v Ecuador*,<sup>864</sup> which resulted in the ignorance of clear dissimilarity of economic sector and the absence of competitiveness between the comparators. On the other hand, an example of case that has over-construed likeness without looking at the situation of investment as a result of the government measure is the case of *UPS v Canada*.<sup>865</sup> In that case, the tribunal scrutinised the minute details of the characters of the investment, such as the manner in which mails and goods arrive so as to differentiate between postal traffic and courier shipments. The tribunal however

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<sup>863</sup> Newcombe and Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (n 65) 165.

<sup>864</sup> *OEPC v Ecuador*, (n 18).

<sup>865</sup> *UPS, Inc v Canada*, (n 21), para 99.

did not construe the relevance of the detailed scrutiny of likeness (despite that those characteristics have been endorsed by international custom experts) to the measure and how would such measure effect the situation of the claimant.<sup>866</sup>

The dilemma is there. By not merging the justification test, the tribunal will be missing an important aspect of assessment if it limits the assessment of likeness at the comparability test.<sup>867</sup> However, by merging, it would be odd to ask the state to justify itself in a case where comparability is not established. It is suggested here, as the cases of *OEPC v Ecuador* and *UPS v Canada* have portrayed, that the oddness will only surface in two situations; firstly if there is clear comparability but ignored, giving way to justification and secondly when there is clear relevance of the justification to the likeness of the investors but ignored, scrutinising the characteristics of the investment.

The balance is ‘relevance’. In the case of *CPI Inc. v Mexico*, the tribunal has correctly assessed likeness independent of justification because the latter brought by the host state was irrelevant to the likeness of the comparators. On the other hand, in the case of *UPS v Canada*, the tribunal should have brought the justification test into likeness to assess the reasonableness of the measure which regarded the comparators as unlike. This would detect the strategies taken by the host states to pursue the

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<sup>866</sup> The tribunal in *UPS v Canada* held that there was no breach of national treatment as the comparators were not in like circumstances. The tribunal analysed the question of likeness between courier and postal traffic in detail in terms of their object, mandate, transport and method of delivery. The claimant alleged less favourable treatment which included denial of brokerage service, exclusion of certain functions, obligation to pay certain costs related to CADEX, payment of penalties and non-enforceability of Customs Law in the postal stream. It appeared that the tribunal has attempted in assessing the likeness of the investments by scrutinising into the differences in detail of an otherwise similar comparators.

<sup>867</sup> In the case of *Methanex v USA*, the tribunal’s assessment did not go beyond likeness test in this case. It has almost abruptly concluded that there was no discrimination after a short consideration of likeness. The discussion evolved mainly around the relevance of GATT/WTO jurisprudence of ‘like product’. *Methanex v USA*, (n 19).

likeness test into detail, independent of the justification test if there is little prospect of defending the latter.

The ECHR jurisprudence allows the examination of the justification of a measure when assessing the comparability of the applicants and their comparators. This, as a result provides no clear demarcation of the steps that comparators should be determined before the justification is perused. Thus the instruments used in assessing likeness rest on the overall situation of the comparators and how likeness of situation of the comparators is affected by the alleged discriminatory measure, and the justification thereof.

### 3.3.3 Proportionality

Generally, the proportionality principle is increasingly accepted in investment decisions.<sup>868</sup> It is seen as an important tool to balance the interpretation of investors' rights in the treaties.<sup>869</sup> While it seems to appear in other substantive principles of the investment treaties, it has not been invoked explicitly in national treatment. Nevertheless, the logic of assessing the execution of legitimate aims proportionately can be seen in several cases. In the case of *CPI Inc. v Mexico for instance*, the tribunal rendered the HFCS Tax was not relevant to the justification brought. The fact that they were being excluded from the US market access which rendered Mexican sugar cane producers not in like situation with HFCS producers (who were

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<sup>868</sup> *Total S.A. v. Argentine Republic*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010; *Saluka Investments BV v. Czech Republic*, (n 251); *Tecnicas Medioambientales Tecmed S.A. v. The United Mexican States*, (n 615).

<sup>869</sup> SB Leinhardt, 'Some Thoughts on Foreign Investors' Responsibilities to Respect Human Rights' (2013) 10 Transnational Dispute Management (TDM) <<http://www.transnational-dispute-management.com/article.asp?key=1927>>, accessed on 25 January 2013.

not barred from the Mexican market) was irrelevant to the decision to impose the HFCS Tax.<sup>870</sup> Although the court would have accepted the crisis of the Mexican sugar industry, the nature of the measure to address the crisis was not reasonably related and was therefore rejected by the tribunal. This was a proportionality approach taken by the tribunal, without which would render all legitimate justifications acceptable without perusing into the manner in which they are executed.

However, the proportionality principle, being not explicit in its cases, is assumed attended to in its assessment of reasonableness. In *SD Myers v Canada*, the tribunal mentioned:

A finding of ‘likeness’ does not dispose of the case. It may set the stage for an inquiry into whether the different treatment of situations found to be ‘like’ is justified by legitimate public policy measures that are pursued in a reasonable manner.

The reasonableness of the manner in which a legitimate aim is pursued would normally be an assessment of proportionality. Thus in the case of *Feldman*,<sup>871</sup> it is hard to demarcate whether proportionality is assessed or neglected. In *Feldman*, the tribunal accepted the rational bases for treating producers and resellers differently, holding that only trading companies are alike, but proportionality was not assessed. In such facts of the case where the investors and the comparator are clearly in the

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<sup>870</sup> *CPI, Inc. v Mexico*, (n 98), para 129.

<sup>871</sup> *Feldman v Mexico*, (n 15), para 170.

tobacco business suggesting likeness to the naked eye, the proportionality test would be extremely vital in determining whether the ruling of unlikeness was proportionate.

Another problem due to the lack of attention towards the principle of proportionality is the vagueness of the standard in investment decisions. In the case of *GAMI v Mexico*, the tribunal was not only lenient (rather, brief or unclear) on what constituted ‘rational’ of the measure, it also seem to suggest ‘ineffectiveness’ as proportionately acceptable. Although the national treatment claim may have failed on lack of evidence or other grounds, the line of decision rings a different and misleading message on the standard of reasonableness and proportionality.<sup>872</sup>

It is suggested that proportionality should be explicitly assessed in national treatment cases. It will not only result to a more systematic judicial interpretation, it could also enhance the legitimacy of the assessment of likeness.

#### **4.0 Analysis of Findings against Analytical Framework**

The analytical framework throughout this research is investment security and reasonableness. The connection between the findings of this research to the analytical framework as laid in the proposal chapter will be explained in this section.

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<sup>872</sup> *GAMI Investments, Inc. v The Government of the United Mexican States, NAFTA/UNCITRAL, Final Award, 15 November 2004*, paras 111-115.

#### *4.1 Investment Security:*

This research has taken into account investment security as the observational standpoint in building the criteria for likeness. It acknowledges that investment security is the overall reason of investment treaties which seek to promote and protect investments by reducing the political risks exposed to foreign investments, mid-sized and multinational companies alike.<sup>873</sup> The hierarchical relation of state and investors grants that host states an advantageous position by the exercise of regulatory powers which could affect foreign investments.

This research promotes investment security by firstly acknowledging it as the underlying philosophy of the investment treaties. The preambles of investment treaties to ‘promote and protect’ investments coupled with its substantives provisions and dispute resolution clauses recognises investment security as the context of interpretation of its clauses. National treatment has to also carry this context in its interpretation.<sup>874</sup>

It is thus important to understand the linkage of investment security and ways to incorporate it in the functioning of the non-discrimination principle. This thesis suggests that the values of national treatment must be made clear; firstly that it promotes level playing field between nationals and non-nationals and secondly, that

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<sup>873</sup> Vandevelde, ‘Economics of Bilateral Investment Treaties, The’ (n 337); Thomas . Walde, ‘Investment Arbitration as a Discipline for Good Governance: Overview and Epilogue’ (2004) 2 Oil, Gas & Energy Law Journal (OGEL) <<http://www.ogel.org/article.asp?key=1180>> accessed 29 April 2013.

<sup>874</sup> The explanation of ‘investment security’ as the analytical framework of this research is explained in Ch.1.

it prohibits nationality based discrimination.<sup>875</sup> These values are the first step towards achieving investment security.

The next important contribution towards investment security is the use of '*effet utile*'.<sup>876</sup> It drives the attention of the tribunal on the objects, purpose, values, effective and reasonable interpretation of national treatment. This would avoid the tribunals from being distracted by specific issues, in particular the determination of likeness, which would lead to a narrow construction of national treatment.

This thesis also recognises the economic situations of investors as a factor of likeness. This is by way of assuming likeness of investments in the existence of competitive relationship. Thus if there is obvious evidence of competitive relationship between the investors, the host states will have to assert stronger evidence that the regulatory measure was necessary to either disprove likeness or justify exceptions.<sup>877</sup>

The situation of investors is the prime area of research in the assessment of likeness. It is thus forwarded in this thesis that, firstly, the tribunal should not confine itself to the narrow characteristic based assessment.<sup>878</sup> Secondly, it must take into consideration both factual and legal circumstances of the investments.<sup>879</sup> Thirdly, it allows the flexibility of independently or merging the assessment of likeness with the regulatory justification, depending on which could serve the most meaningful

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<sup>875</sup> See 'Lesson Learnt 1: The Values of National Treatment' in 2.0 above.

<sup>876</sup> See '*Effet Utile*' in 3.2.2 above.

<sup>877</sup> See 'Competition Test' in 3.1.1 above.

<sup>878</sup> See 'Emphasis on the 'Situation' of the Comparators' in 3.2.1 above.

<sup>879</sup> *Ibid.*



assessment.<sup>880</sup> All of these factors are supporting investment securities in the interpretation of national treatment contributed by this research.

#### 4.2 Reasonableness:

This thesis has observed how the GATT/WTO, EU and international human rights jurisprudence consider reasonableness in the jurisprudences. The EU law for instance requires that the challenged measure must be ‘objectively comparable’ or be justified by ‘overriding reasons in the general interest’.<sup>881</sup> GATT/WTO promulgates reasonableness by the requirement that measures must not constitute “means of arbitrary or unjustifiable discrimination”<sup>882</sup> while the international human rights jurisprudence highlights measure to have ‘objective and reasonable justification’<sup>883</sup>.

Similarly, investment treaties do not prohibit states from exercising its policy space to create regulations. They must however be done in conformity to the international obligations and genuinely representing public issues that the states face as sovereigns. International investment arbitration thus could not be treated as any other commercial arbitration.<sup>884</sup> Due to the broadness of investment treaties (in particular

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<sup>880</sup> See ‘Practicality of the Three Prong Test of National Treatment in the Determination of Comparators’ in 3.3.2 above.

<sup>881</sup> *Manninen*, (n 529) para 28 and 20, Case C-35/98, *Verkooijen*, (n 555) para 43 and Case C-512/03, *J.E.J. Blanckaert v Inspecteur van de Belastingdienst/ Particulieren/ Ondernemingenbuitenlandte Heerlen*, para 42.

<sup>882</sup> GATT, Article XX.

<sup>883</sup> *Darby v Sweden*, (App.11581/85), 23 October 1990, Series A, No 187, (1991) 13 EHRR 774, para 31; *Chassagnou and Others v. France* [GC], nos. 25088/94, 28331/95 and 28443/95, ECHR 1999-III, para 91; *Spadea and Scalabrino v Italy* (App. 12868/87), 28 September 1995, para 46.

<sup>884</sup> William Burke-White and Andreas von Staden, ‘The Need for Public Law Standards of Review in Investor- State Arbitrations’ in Stephan W Schill (ed), *International Investment Law and Comparative Public Law* (OUP Oxford 2010). See also Schill, ‘Rethinking the Substantive Standards of Protection under Investment Treaties – How Much Deference Should Investment Treaty Tribunals Pay to the Regulatory or Judicial Acts of Host States?’ (n 851).

the national treatment provision) and the absence of defined exceptions in most investment treaties that could assist interpretation,<sup>885</sup> there is more need for public law concepts that could enhance good governance.<sup>886</sup> The application of reasonableness should therefore be regarded as a norm. On this note, the framework of this analysis is to ensure that the interpretation of national treatment must be grounded on this concept.

Operationally, reasonableness is taken into account in the assessment of likeness in this thesis in at least two functions, as a tool and as an end, sometimes interchangeably. It is as a tool to balance the complex conflicts of interests between the investors and host states. It is particularly a core tool to assess the legitimacy of the regulatory measure. What is deemed reasonable must be considered by the tribunal as to its legitimacy. Here, the tribunal must acknowledge that there are reasonable grounds that the host states should be allowed to put forth to discriminate local and foreign investors considering its public role in representing the people. This can be done by the conferment of margin of appreciation to the host states.<sup>887</sup> As Chapter Five has extensively discussed, the conferment of margin of appreciation to the host state could ensure that matters of public interest within the state's specific socio-economic interest are addressed.

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<sup>885</sup> Such as Article XX in GATT/WTO.

<sup>886</sup> This is considering that investment law is not mere commercial disputes. See Benedict Kingsbury and Stephan Schill, 'Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest—the Concept of Proportionality' in Stephan Schill (ed), *International Investment Law and Comparative Public Law* (Oxford University Press 2010).

<sup>887</sup> See 'Margin of Appreciation' in 3.3.1 above. Deference is essential to investment arbitrations due to its public nature. See Schill, 'Rethinking the Substantive Standards of Protection under Investment Treaties – How Much Deference Should Investment Treaty Tribunals Pay to the Regulatory or Judicial Acts of Host States?' (n 851); Anthea Roberts, 'The Next Battleground: Standards of Review in Investment Treaty Arbitration' (2011) 16 *International Council for Commercial Arbitration Congress Series* 170–180.

Reasonableness again steps in to determine the relevance and appropriateness of the execution of the measure to the issue at question. This thesis suggests that the principle of proportionality could fortify this function of reasonableness.<sup>888</sup> The principle of proportionality has not been taken as a clear requirement in the investment disputes. There are thus risks that it may be overlooked by the tribunals. It is suggested in this thesis that it should be the final filter that the tribunal must ascertain before a measure is considered legitimate.<sup>889</sup>

It functions as an end to allow the tribunal to analyse the plausibility of the outcome of the adoption of a particular methodology or interpretation. It is submitted that the outcome of an investment decision must be perceived as just. One way to do this is for the tribunal to adopt the ‘relevance’ test in deciding whether to adopt the independent three prong likeness test or the merging of justification approach in determining likeness.<sup>890</sup> It is also important for the tribunals to understand the dynamics of the assessment likeness if the facts are near or moving away from the factors such as similar economic sector, competition and protectionism.<sup>891</sup>

#### **4.0 Coherence and Legitimate Expectation**

The significance of this research is that it promotes coherence in the interpretation of national treatment.<sup>892</sup> This research could be a significant guideline in understanding the application of the national treatment provision. The coherence of criteria to

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<sup>888</sup> See ‘Proportionality’ in 3.3.3. above.

<sup>889</sup> See ‘Criteria of Likeness in International Investment Law: A Suggested Approach’ in 6.0 below.

<sup>890</sup> See ‘Practicality of the Three Prong Test of National Treatment in the Determination of Comparators’ in 3.3.2 above.

<sup>891</sup> See ‘Criteria of Likeness in International Investment Law: A Suggested Approach’ in 6.0 below.

<sup>892</sup> See 6.1 in Ch.1.

assess likeness will in turn create legitimate expectation for both the state and the investors. This thesis pushes this by arguing that the decisions of the investment tribunals are able to develop a coherent jurisprudence on national treatment and could then result to a set of legitimate expectation in which host states should act in accordance to.

Legitimate expectation is formed on two bases: Firstly, by signing investment treaties which provides national treatment, it creates legitimate expectation that foreign investors shall be treated in an unbiased manner. Thus where the host state has provided a particular regulatory atmosphere in which investors expectedly rely on, it will be against legitimate expectation if it is modified or interfered by providing less favourable treatment to foreign investors.<sup>893</sup> Secondly, building from the first argument, it is submitted that the doctrinal embodiment and the underlying philosophies of national treatment which influences its interpretation should constitute legitimate expectation as a part of coherence and legitimacy.

This section primarily explains the second basis of legitimate expectation by accumulating the findings of this thesis.

Firstly, the national treatment principle is intended to discipline states only if states introduce unjustified protectionist measures. Protectionism without justification will be an indicator an irrational measure and thus a state could not use the same justification to conclude that the investors are not in like circumstances. Whenever there is evidence of protectionism, the burden of proof will shift to the state to show

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<sup>893</sup> *Mesa Power v Canada*, (n 749). See also Footer, 'On the Laws of Attraction: Examining the Relationship between Foreign Investment and International Trade' (n 318) 131.

that there is legitimate reason for such measure. The existence of discrimination against nationality can be deduced from the structure of the measure and the disparate impact on the foreign investors.

Secondly, investments in the same economic sector and in competition with each other will likely be assumed as in like circumstances. Any justification brought by the state must be of overriding public interest, reasonable and proportionate to be able to negate likeness or to justify discrimination.

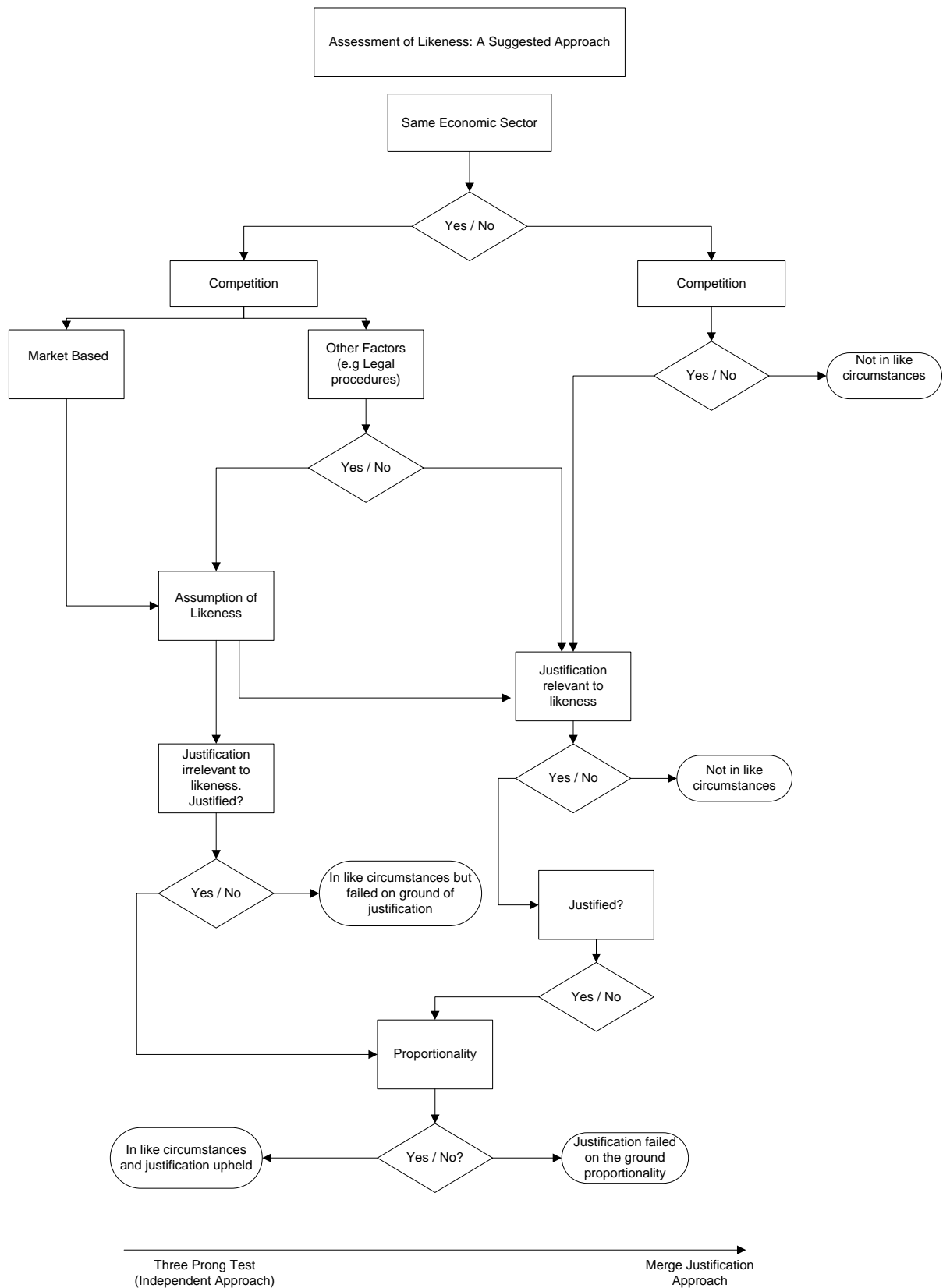
Thirdly, it must be acknowledged that host states have a wide margin of appreciation if the measure involved issues of genuine public interest, for instance health, environment, economic necessity and safety. This margin of appreciation can conclude that investments are not in like circumstances. The margin of appreciation given to the states must be restricted based on the principle of reasonableness and proportionality.

By having such coherence, investors could predict the outcome of a case if they wish to challenge a discriminatory measure under national treatment. Similarly host states could also regulate within its legitimate sphere based on the same legitimate expectation. This will avoid cases being brought for arbitration on meritless grounds that would save the consumption of time and money.

## **6.0 Criteria of Likeness in International Investment Law: A Suggested Approach**

As a summary of the discussions, this research provides a flowchart in which national treatment cases should be construed to determine likeness. This chart will incorporate the legitimate expectations in the previous section and suggests the situations in which the three prong test or the merged justification test could appropriately be applied. This chart assumes that less favourable treatment is already accorded to the foreign investors (as in the first step of the three prong test) and proceeds at examining the question of likeness and justification. The explanation of the chart will indicate the lessons learnt taken from GATT/WTO, EU and the international human rights jurisprudence and reaffirms plausible methodologies already applied in investment tribunals.

The flowchart is as the following:



The first enquiry is whether the comparators are in the same economic sector. Similarity in the economic sector is the most plausible starting point for assumption of likeness. This is due to the high possibility that investors in the same economic sector are likely to be in competition or face similar regulatory measures and business situations. The NAFTA cases of *Pope & Talbot v Canada* and *SD Myer, Inc. v Canada* are in line with this approach. This is a unique approach in international investment law. In *Pope & Talbot* the tribunal upheld,

‘In evaluating the implications of the legal context, the Tribunal believes that, as a first step, the treatment accorded [to] a foreign owned investment protected by Article 1102(2) should be compared with that accorded domestic investments in the same business or economic sector.’<sup>894</sup>

The same question is not asked in GATT/WTO, EU nor the international human rights jurisprudences. In GATT/WTO for instance, the enquiries are whether the products are similar. Taking into account the economic nature of investment treaties, it is therefore plausible to construe likeness within the same economic sector as the first enquiry.

Next is the issue of competition. Investments in the same economic sector may or may not be in competition with each other. The test applied here is whether the comparators are in competition of investment opportunity.<sup>895</sup> In order to encompass the wide range of investment activities, it is submitted that investment opportunities

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<sup>894</sup> *Pope & Talbot v Canada*, (n 20), para 78. See also *SD Myers, Inc. v Canada*, (n 24), para 250.

<sup>895</sup> See ‘Level Playing Field’ in 2.1 above.



can be further categorised into market-based competition and non-market based competition. The first category involves similar economic activities, often the same products as the subject of investments as trade. This often involves investments in the manufacturing sector. This is exactly the overlapping area that may invoke cases under both regimes.<sup>896</sup> A single policy may affect both trade and investments.<sup>897</sup> If the comparators are competing in the same market and the same consumers, it is submitted that this must result in assumption of likeness.<sup>898</sup>

The reality of competition of investment opportunities is not confined to the proceeds of sales in the market. Other factors that may impede competitiveness of investments are, for instance, exemptions of certain procedural requirements, grant or retraction of permits and imposition of certain taxes that may cause less favourable situations for foreign investors in the same economic sector. There are many types of foreign direct investments that may not involve direct competition in sales or services especially those in the extractive industries or infrastructure.<sup>899</sup> A case to illustrate a situation of investments in the same economic sector but not competing in a market-based competition is *Bayindir v Pakistan*. The investment opportunities competed was the more favourable construction schedule and similar (lenient) treatment in the PMC-JV's unsatisfactory performance.<sup>900</sup> Similarly, in the

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<sup>896</sup> *ADM v Mexico*, (n 355); *CPI, Inc v Mexico*, (n 98) and *Methanex v USA* (n 19). See also Tania C Voon and Andrew D Mitchell, 'Time to Quit? Assessing International Investment Claims Against Plain Tobacco Packaging in Australia' (2011) 14 *Journal of International Economic Law*, for possible trade and investment claims against plain tobacco packaging.

<sup>897</sup> Debra P Steger, 'International Trade and Investment: Towards a Common Regime?' in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (2013) 159.

<sup>898</sup> See further discussion on competition as a criterion of likeness and relevant cases in 'Competition Test' in 3.1.1 above.

<sup>899</sup> Theodore H. Moran, 'Foreign Direct Investment and Development: Novel Challenges' in Roberto Echandi and Pierre Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (Cambridge University Press 2013) 42.

<sup>900</sup> *Bayindir v Pakistan*, (n 290), para 393.

case *Parkerings v Lithuania*, both of the investments compete the bid to construct the two multi-storey car park system (the ‘MSCP’) in the City of Vilnius.<sup>901</sup> The claimant purported that,

‘In the Claimant’s view, the Companies Pinus Proprius and BP were facing similar circumstances. The refusal of the City of Vilnius to sign a JAA or a Cooperation Agreement prevented BP from the construction of any MSCP in Vilnius and thus deprived it of the opportunity to carry out its investment as it was entitled to do under the Agreement.’

This was the subject of the competition. In situations or clear competition like this, the tribunal should assume likeness if there is no justification brought by the host state that could negate it.<sup>902</sup>

Once the tribunal has arrived at this stage, the tribunal should assess whether there are justifications of the regulatory measure brought by the host state that are relevant to the assessment of likeness. If the justification is relevant to the assessment of likeness, the tribunal should adopt the merge justification test and determine the legality of the regulatory distinction. In this case, the assumption of likeness is withheld until the legitimacy of the distinctive regulatory is ascertained. At this point, the burden of proof on the host states is higher so as to be convincing enough

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<sup>901</sup> This claim was brought under most favoured nation principle, but it could nevertheless shed some light in the interpretation of national treatment.

‘*Most-favoured-nation (MFN)* clauses are by essence very similar to “*National Treatment*” clauses. They have similar conditions of application and basically afford indirect advantages to their beneficiaries, namely a treatment no less favourable than the one granted to third parties. Tribunals’ analyses of the *National Treatment* standard will therefore also be useful to discuss the alleged violation of the *MFN* standard.’

See *Parkerings v Lithuania*, (n 257), para 366.

<sup>902</sup> The host state in both *Bayindir v Pakistan* and *Parkerings v Lithuania* brought justifications to negate likeness which was accepted by the tribunal. This will be discussed in the following paragraphs.

against the assumption of likeness of investments in the same economic sector. Taking the same case of *Bayindir v Pakistan*, the tribunal took into consideration the difference in experience and expertise of the foreign investor and local competitor so as to render the investments not in like circumstances.

‘The expertise and experience of the contractors constitutes another difference. Bayindir benefited from considerable experience in handling large projects, while PMCJV did not. This difference which was reflected in the higher rates charged by Bayindir, played a role in the expectations that NHA formed with respect to each contractor.’<sup>903</sup>

This justification was relevant to the assessment of likeness and therefore the tribunal has correctly adopted the merge justification test. The investors are deemed alike only if the differences of the regulatory measure are unjustified. In a similar vein, the tribunal in *Parkerings v Lithuania* asserted:

‘However, the situation of the two investors will not be in *like circumstances* if a justification of the different treatment is established.’<sup>904</sup>

The tribunal in *Bayindir* has considered the reasonableness of the distinctions, judging from the considerations of lack of expertise, experience, foreign currency component, mobilization advance and the old equipment, machinery and plant,<sup>905</sup> but had not regarded the proportionality of the measure. The decision may probably be the same had proportionality be evaluated, but a clearer and systematic assessment

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<sup>903</sup> *Bayindir v Pakistan*, (n 290), para 410.

<sup>904</sup> *Parkerings v Lithuania* (n 257), para 375.

<sup>905</sup> *Bayindir v Pakistan*, (n 290), paras 403-411.

on the reasonableness and proportionality of the measure even if the case fails on the account of likeness test would contribute to a more reasoned award.

The case of *Parkerings v Lithuania* has probably shown an extent of systematic analysis in merge of justification case.<sup>906</sup> It explicitly highlighted the importance of reasonableness and proportionality in discrimination cases:

‘However, to violate international law, discrimination must be unreasonable or lacking proportionality, for instance, it must be inapposite or excessive to achieve an otherwise legitimate objective of the State. An objective justification may justify differentiated treatments of similar cases. It would be necessary, in each case, to evaluate the exact circumstances and the context.’

In the assessment of the reasonableness of a regulatory distinction, the tribunal must take due regards to the probability of protectionist purpose which is not backed by reasonable justifications.<sup>907</sup> If the measure is legitimate, the comparators are declared not in like circumstances because of the distinctive regulation.

If the justification is independent from the assessment of likeness (such as in the case of *CPI Inc. v Mexico*), the tribunal could then pursue to determine the legitimacy of the regulatory measure once likeness is declared. This is generally the model taken from Article XX GATT/WTO which examines the legitimacy of the regulatory

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<sup>906</sup> *Parkerings v Lithuania* (n 257), paras 375-396.

<sup>907</sup> See discussion on protectionism in ‘Nationality Based Discrimination’ in 2.2 above.

measure at a later stage.<sup>908</sup> This is also the three-prong test approach suggested in the case of *Pope v Talbot, Inc v Canada*<sup>909</sup>. The process of determining whether the merge of justification approach or the three-prong test approach is important, firstly to declare likeness at its right stage and secondly, to avoid tribunals from being allured to the politicising of this grey area by the parties.<sup>910</sup>

If the justification in the three prong test is not accepted by the tribunal, the tribunal can then conclude that the comparators were ‘in like circumstances but failed on the ground of justification’. In cases where justifications of the host states are accepted, the tribunal must countercheck its proportionality. If the justification passes the proportionality test, then there is no breach of national treatment. If it does not, the tribunal will conclude that the justification failed on the ground of proportionality. The latter is not construed well in investment arbitrations. It is assumed that the tribunal will consider proportionality in the justification test. There is a risk that the tribunal may overlook it.<sup>911</sup> This is also an important tool to balance the margin of appreciation applied by the host state. This is also an important lesson learnt from the international human rights jurisprudence, in particular the ECHR, which explicitly asserts the role of proportionality in its discrimination assessment but nevertheless seems to neglect it in providing margin of appreciation to the states.<sup>912</sup>

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<sup>908</sup> Legum and Petculescu, ‘GATT Article XX and International Investment Law’ (n 319)

<sup>909</sup> *Pope v Talbot, Inc v Canada* (n 20).

<sup>910</sup> The international human rights law in particular has shed some light in the plausibility of the merge of justification approach in some cases to derive at a more meaningful interpretation of likeness. It has also in some scholarly articles highlighted the threat of such a method being politicised to favour a certain argument. See Cornides, ‘Three Case Studies on Anti-Discrimination’ (n 711).

<sup>911</sup> See the case of *GAMI v Mexico* discussed in ‘Proportionality’ in 3.3.3 above.

<sup>912</sup> The problems with excessive use of margin of appreciation if not counterchecked by the principle of proportionality is explained in Ch.5.

Moving to the right hand side of the graph, this thesis does not limit the possibility of likeness to investments which are in the same economic sector. Investments which are not in the same economic sector may still compete the same investment opportunities.<sup>913</sup> A few examples are; regulatory measures that affect a broader group of economic sectors such as labor requirements which affect garments or footwear investments, measures for a particular geographical catchment or environmental regulations that may affect infrastructure investments and power projects alike.

It must be cautioned that the assessment of likeness in these cases will involve heavy scrutiny. It is particularly in these types of cases that the claimant must show that there is discrimination based on nationality based on the overall structure and effect of the regulatory measure. The tribunal must be careful of the possibility of declaring likeness in broad range of comparators unless there is reasoned analysis that leads to that conclusion.

Cases that have attempted to invoke this are *El-Paso v Argentina* and *OEPC v Ecuador*. In *El-Paso v Argentina*, the claimant asserted that their investment in the energy sector was in like circumstances with investments in the banking sector. There was strict scrutiny in determining whether the comparators were in like circumstances. The tribunal took into consideration the factual disadvantaged position of the banking sector as a result of asymmetrical pesification and the government's effort to correct the situation. This is a respectable approach taken.

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<sup>913</sup> In a similar vein, Walde has highlighted the possibility of legitimate comparison across borders, depending on the design of the measure that aims for lesser treatment of foreign investors. See Walde, 'Comments on the Discipline of 'National Treatment: Boosting Good Governance and Intruding into Domestic Regulatory Space?' (n 3).

However, it is submitted that the tribunal's less meticulous attention to the relevance of the nationality based discrimination is both undesirable and confusing. It is hard to draw a balance in the tribunal's approach that on the one hand it did not accept that there must be a finding of discriminatory intent, but on the other unconvinced that the measure which affected the energy sector was part of a specific policy to discriminate.<sup>914</sup> The tribunal seemed to take into account the former for the finding of the latter. Had the tribunal construed its analysis on the structure and factual circumstances of the measure in light of nationality based discrimination (as suggested by this thesis), it would have released the tribunal from the apprehension that discriminatory intent was necessary that should be avoided.

The case of *OEPC v Ecuador* has received vast criticism in this aspect. The tribunal did not pay attention to the absence of discriminatory motive based on nationality but rather gave the benefit of likeness to the claimants despite being in different economic sectors. Decisions such as this require reasoned justifications as it is more the exception than the rule.

Generally, from the discussion above it can be concluded that it is harder to prove likeness when it involves comparators of different economic sectors. The merge of justification test is more likely to be applied when the facts of the cases move away from the same economic sector. Relatively, cases falling under the three prong test are straightforward and easier. Where the merge of justification test is applied, there will be more room for margin of appreciation for the host states and in turn, the proportionality assessment will be more rigorous.

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<sup>914</sup> *El-Paso v Argentina*, (n 173), paras 305-308.

## **7.0 Conclusion**

The study reveals that there is more to the interpretation of likeness in national treatment provisions than it seems. It is a fascinating subject, alive and involves important stakes, a fertile ground for private and public interests to interact. It can also be regarded as both the strength and the Achilles of the national treatment provision, depending on how the interpretation is directed to. It is under this realisation that this thesis aims to bring the interpretation of national treatment to what is just in terms of the obligation to foreign investors and what is right in the function of the sovereigns and the people.

This thesis has responded to this complexity by understanding most importantly what obligation the host states have in the national treatment provision. This is translated into the underlying values of national treatment as described in this chapter. It has firstly identified two important underlying values of national treatment which are, firstly to ensure level playing field and secondly, to protect foreign investors against unreasonable nationality based measures. These findings are deduced from the doctrinal evaluation of the objectives and purposes of the investment treaties, the tribunals' construction of investment cases and the reflection from the notion of national treatment under the jurisprudences under comparison, namely GATT/WTO, EU and international human rights law. This chapter summarised the essence of the national treatment provision in investment agreements. It captured the lessons learnt from the jurisprudences under comparison and operationalises them in the assessment of likeness in national treatment under international investment law.



Putting the underlying values of national treatment in place, it is then apt to determine the role of likeness in the provision. The analysis comprises lessons learnt from GATT/WTO, EU and International Human Rights Law in particular the role of ‘competition’, ‘protectionist purpose’, ‘aims and effect test’, ‘situation’ of the comparators, the ‘*effet utile*’ of the jurisprudence, the importance and limits of ‘margin of appreciation’ and the consequences of adopting the ‘independent or merge of justification test’ in assessing likeness. This chapter has assimilated the lessons learnt into the context of investment law by way of revisiting investment cases and suggesting its way forward.

This thesis has considerably portrayed the complicated position of the international investment regime in responding to public concerns in national treatment cases. It has promoted the adaption of administrative public law principles such as the principles of ‘reasonableness’ and ‘proportionality’ and supported the relevance of ‘margin of appreciation’ in the interpretation of likeness. This is the most sustainable way in which investment law could move forward, enhancing its legitimacy and acceptance.<sup>915</sup>

In conclusion, this thesis develops a body of knowledge on the interpretation of likeness and its relevant counterpart -the determination of legitimate regulatory measures- in national treatment. It provides the criteria and guidelines in which likeness should be interpreted, highlighting the ‘circumstances’ or ‘situations’ of the

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<sup>915</sup> Kingsbury and Schill, ‘Public Law Concepts to Balance Investors’ Rights with State Regulatory Actions in the Public Interest—the Concept of Proportionality’ (n 886); Stephan W. Schill, ‘The Public Law Challenge: Killing or Rethinking International Investment Law?’ [2012] Columbia FDI Perspectives.

investments and the economic context of the investment treaties. It has provided the methodologies in which situation the determination of legitimate regulatory measures becomes relevant to the interpretation of likeness. In the determination of legitimate regulatory measure itself, it has posed the importance of deference, balanced with the principles of reasonableness and proportionality. The comparative study involving the GATT/WTO, EU and international human rights law has proven fruitful in providing insights for the direction of interpretation of likeness. It is concluded that these jurisprudences are relevant to the interpretation of likeness. This comparative study is an academic effort for the development of the doctrinal embodiment of national treatment and is hoped to be influential in the practical arena.

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